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No. 06-____

IN THE

Supreme Court of the United States

BERNARD J. EBBERS,

Petitioner,

v.

UNITED STATES OF AMERICA,

Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Second Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

At petitioner's trial, the government granted use immunity to eight prosecution witnesses. The government used those witnesses to introduce out-of-court statements of three alleged co-conspirators. When petitioner subpoenaed the alleged co-conspirators, they indicated that they would assert their Fifth Amendment privilege to avoid testifying. Petitioner then moved to compel the government to grant them use immunity—on the grounds that their testimony would contradict the out-of-court statements, impeach the prosecution witnesses, and offer exculpatory evidence—or face dismissal of the indictment. The district court denied petitioner's motions. The district court also instructed the jury that it could convict petitioner of "willfully" and "knowingly" engaging in conspiracy and securities fraud if it found that he was aware of a "high probability" of fraud at his company but "consciously avoided confirming" it. The Second Circuit affirmed.

The Questions Presented are:

1. Whether a trial court may require use immunity for defense witnesses whose testimony would contradict their purported out-of-court statements, impeach immunized prosecution witnesses, or offer exculpatory evidence.

2. Whether appellate courts should review district court decisions on defense witness immunity *de novo* or for abuse of discretion.

3. Whether the trial court erred in giving the jury a "conscious avoidance" instruction where the relevant statutes require proof of actual knowledge, there was no evidence the defendant avoided knowledge for the purpose of building a defense to prosecution, and the government relied on the same evidence to prove both actual knowledge and, alternately, conscious avoidance of actual knowledge.

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Bernard Ebbers respectfully petitions this Court for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit.

OPINIONS BELOW

The court of appeals' opinion is reported at 458 F.3d 110 (2d Cir. 2006) (Pet. App. 1a). The decisions of the district court are not reported. The following district court rulings are reproduced in the appendix: July 9, 2005 order denying motion for a new trial (Pet. App. 42a); February 25, 2006 denial of Ebbers' renewed motion for defense witness immunity (Pet. App. 83a); November 10, 2004 denial of motion for defense witness immunity (Pet. App. 85a); February 25, 2005 charge conference (Pet. App. 105a); March 2, 2005 ruling on conscious avoidance charge (Pet. App. 107a); and March 4, 2005 conscious avoidance instructions (Pet. App. 110a).

JURISDICTION

The judgment of the court of appeals was entered July 28, 2006. This Court has jurisdiction under 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISIONS, STATUTES, AND REGULATIONS INVOLVED

The following constitutional provisions, statutes, and regulations are reproduced in the appendix: the Fifth and Sixth Amendments to the United States Constitution; 15 U.S.C. §§ 78ff, 78j(b), 78m(a); 18 U.S.C. §§ 2, 371, 6001-6003; and 17 C.F.R. §§ 240.10b-5, 240.13a-1. Pet. App. 92a.

PRELIMINARY STATEMENT

For decades, lower courts have been divided over whether and under what circumstances courts may require use immunity for defense witnesses. All the circuits have addressed these questions numerous times, and yet the lower

courts have only grown more divided.[1] These issues are of vital importance, particularly in conspiracy cases. Prosecutors often grant use immunity to alleged co-conspirators to obtain testimony favorable to the government. Simultaneously, they inform other persons with evidence favorable to the defendant that they are potential targets of investigation and refuse to grant them use immunity. When those persons are called by the defense, they assert their Fifth Amendment privilege and refuse to testify. The result is that the defendant is unable to present crucial evidence.[2] The unfairness is especially manifest where, as here, the proposed defense witnesses would directly contradict the government's immunized witnesses.

Similarly, the circuits have long been divided over when a trial court may give a conscious avoidance jury instruction where a statute requires proof that the defendant acted knowingly. Most circuits have recognized the inherent risk that such an instruction can permit a jury to convict on the ground that the defendant *should* have known something, rather than

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[1] Justice Marshall cited the split in the circuits 22 years ago as warranting certiorari. *Autry v. McKaskle*, 465 U.S. 1085, 1087-88 & n.3 (1984) (Marshall, J., dissenting from denial of certiorari) ("'The Supreme Court has not decided whether courts may grant defense witnesses use immunity, and the circuit courts which have addressed the issue have produced widely divergent opinions.'") (*quoting United States v. Thevis*, 665 F.2d 616, 639 (5th Cir. 1982)). At the time, there were generally two conflicting approaches. *See United States v. Angiulo*, 897 F.2d 1169, 1190 (1st Cir. 1990) ("A number of our sister circuits have considered this question, and two theories have emerged."). Today, as discussed *infra* pp. 12, there are at least three conflicting approaches.

[2] *See, e.g., United States v. Skilling*, Crim. No. H-04-0254, 2006 U.S. Dist. LEXIS 42664, at * 24-25 (June 23, 2006) (denying defendants' motion for defense witness immunity while suggesting that the result might have been different in Ninth Circuit), *vacated in part on other grounds, United States v. Lay*, No. H-04-0025, 2006 U.S. Dist. LEXIS 75193, at *19 (S.D. Tex. Oct. 17, 2006).

that he *actually* knew it. But they remain deeply split over the test for determining when the instruction may be given.

On both issues, the Second Circuit has adopted the standard most harmful to defendants' constitutional rights. The application of those standards in this case prevented Ebbers from offering crucial evidence in his defense, and allowed the jury to convict without having to find the *mens rea* required by statute. Had the government prosecuted Ebbers in another circuit, the district court's decisions on these issues—and the result in this case—would have differed.

STATEMENT OF THE CASE

Bernard Ebbers was the Chief Executive Officer of WorldCom, a telecommunications company. In the late 1990s, WorldCom experienced regular annual revenue growth. Tr. 1882.[3] Anticipating continued growth, WorldCom entered into long-term leases of telecommunications lines with third parties to ensure adequate network capacity for its customers. Tr. 2081-82. In 2000, the "dot com bubble" burst, resulting in the bankruptcy of a number of WorldCom's Internet customers. This slowed WorldCom's revenue growth. Tr. 1884. But because of its long-term line leases, WorldCom's expenses did not decrease to the same degree. Tr. 2082. Between 2000 and 2002, WorldCom Chief Financial Officer Scott Sullivan and members of the accounting department made accounting adjustments to WorldCom's line-cost expenses and revenues. Tr. 2085-88, 1936-38, 2034-36. The government, alleging that these adjustments were fraudulent, indicted Sullivan and four other former WorldCom employees in 2002 for conspiracy, securities fraud, and related offenses. All five pleaded guilty.

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[3] "Tr." refers to the trial transcript. "J.A." refers to the joint appendix. "S.A." refers to the sealed appendix filed with the Second Circuit.

A. District court proceedings

On May 24, 2004, the grand jury returned a nine-count superseding indictment against Ebbers, charging that he willfully and knowingly conspired to commit securities fraud, made false statements in SEC filings, and falsified WorldCom's books and records.[4] The government contended that Ebbers, Sullivan, and other members of management concealed WorldCom's true operating performance from the public and reported financial results based on fraudulent accounting. At trial, the government sought to prove that WorldCom fraudulently decreased its line-cost expenses and fraudulently recognized revenue for allegedly "one-time" or "nonrecurring" items without separately disclosing any changes in its accounting methods in its financial statements.

1. Defense Witness Immunity

The government made extensive use of various forms of use immunity to obtain testimony from eight former WorldCom employees. It entered into cooperation agreements with the five witnesses, including Sullivan, who had pleaded guilty; made non-prosecution agreements with two other witnesses; and conferred statutory use immunity on another witness.[5] Under these arrangements, the witnesses testified at Ebbers' trial, but the government could not use that testimony or evidence derived therefrom in any subsequent criminal proceedings against them.[6]

The government's case against Ebbers rested primarily

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[4] 18 U.S.C. § 371 (Count One); 15 U.S.C. §§ 78j(b) & 78ff and 18 U.S.C. § 2 (Count Two); 15 U.S.C. §§ 78m(a) & 78ff and 18 U.S.C. § 2 (Counts Three through Nine).

[5] 18 U.S.C. §§ 6002-6003.

[6] *See Kastigar v. United States*, 406 U.S. 441, 442 (1972).

on Scott Sullivan's testimony that he told Ebbers several times that WorldCom could meet its financial targets only through accounting that "wasn't right" and that Ebbers replied that the company had to "hit our numbers." Tr. 1951. The government used its other immunized witnesses to try to corroborate Sullivan's testimony.

In particular, Sullivan and two other government witnesses testified as to purported out-of-court statements by three other WorldCom executives: Ronald Beaumont, Stephanie Scott, and Ronald Lomenzo. The government had not—and never has—charged Beaumont, Scott, or Lomenzo with any crime. Nevertheless, the government named them as "unindicted co-conspirators." Accordingly, the district court allowed the government's witnesses to testify as to Beaumont's, Scott's, and Lomenzo's out-of-court statements on the ground that co-conspirator statements are not hearsay. Tr. 3612-15. These co-conspirator statements ostensibly corroborated Sullivan's testimony by making it appear that Ebbers and members of management beyond Sullivan and the accounting department participated in the fraud.

Ebbers subpoenaed Beaumont, Scott, and Lomenzo to testify in his defense. All three, however, invoked their Fifth Amendment privilege against self-incrimination. When the government refused to grant them use immunity, Ebbers moved for a court order compelling the government to grant them immunity or face dismissal of the indictment. Ebbers also moved, in the alternative, for a hearing on his request.

Ebbers proffered statements that Beaumont, Lomenzo and Scott had made in interviews with internal investigators and with FBI agents. J.A. 91, 99, 123; S.A. 8, 19, 22, 30, 32, 41, 47. These statements, Ebbers argued, indicated that the three witnesses would deny making the statements attributed to them by the government's immunized witnesses, impeach the credibility of the government's witnesses, and offer exculpatory evidence. J.A. 84; S.A. 2-5.

The district court denied Ebbers' motion, relying on Second Circuit precedent holding that there is a "'general rule'" against defense witness immunity and that an exception applies only if the defendant shows that "'the government has engaged in discriminatory use of immunity to gain a tactical advantage.'" Pet. App. 86a. The court held that Ebbers failed to meet this standard, relying in part on an *ex parte* declaration by the prosecutor, submitted *in camera*, that Ebbers' proposed witnesses were potential targets of investigation. Pet. App. 88a. The court held that, under Second Circuit precedent, such a declaration "'foreclose[s] any inquiry concerning immunity for that witness.'" Pet. App. 90a. The court later reiterated this holding in denying Ebbers' request for a new trial, quoting Second Circuit precedent instructing trial judges to "'summarily reject claims for defense witness immunity whenever the witness for whom immunity is sought is an actual or potential target of prosecution. No hearing should be held to establish such status.'" Pet. App. 60a. To this day, neither Ebbers nor his attorneys have ever been permitted to see the *ex parte* declaration.

Unable to obtain their testimony, Ebbers moved to use Beaumont's, Lomenzo's, and Scott's prior statements to impeach the statements attributed to them by the government's witnesses. The district court denied that motion with respect to all of the statements except one. Tr. 3612-15.[7]

Ebbers testified in his own defense. He denied knowledge of any fraud and disputed Sullivan's claims about their supposed one-on-one conversations. Tr. 3717-20, 3742-43.

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[7] The court also rejected Ebbers' request for a "missing witness" instruction, which would have permitted the jury to infer that the witnesses' testimony would have been unfavorable to the government if it found that the government was in the best position to call them. Pet. App. 68a. It also prohibited Ebbers' attorney from referring to the absence of the witnesses in closing argument. Tr. 4087-90.

In its closing argument, the government prominently featured out-of-court statements attributed to Beaumont and Scott. The government even included two statements attributed to Beaumont in its "Top 10" list of evidence against Ebbers. Tr. 4242-43.

2. Conscious Avoidance Jury Instruction

Over Ebbers' objection, the court gave the jury two "conscious avoidance" instructions, which allowed the jury to convict if it found "that the defendant was aware that there was a high probability of a fact, but that the defendant deliberately and consciously avoided confirming this fact." Tr. 4444, 4456. While knowledge is an element of each count in the indictment, the instruction enabled the jury to "treat his deliberate avoidance of positive knowledge as the equivalent of knowledge." Tr. 4444-45, 4456. Applying Second Circuit precedent, the district court held that the instructions were warranted because Ebbers' "involvement in the fraudulent scheme was 'so overwhelmingly suspicious' that his 'failure to question the suspicious circumstances establishes [his] purposeful contrivance to avoid guilty knowledge.'" Pet. App. 50a (citation omitted); Pet. App. 48a.

3. Verdict and Sentencing

After deliberating for eight days, the jury returned guilty verdicts on all counts. The district court sentenced Ebbers to 25 years' imprisonment.[8]

B. Second Circuit Decision

The Second Circuit affirmed. While acknowledging a circuit split on the appropriate standard of review, the Second

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[8] The court acknowledged that this was "likely to be a life sentence" given Ebbers' age, 65, and serious heart condition. J.A. 530-31. In contrast, Sullivan was sentenced to five years, and the other cooperating witnesses to terms ranging from probation to one year and one day.

Circuit reviewed the district court's decisions on defense witness immunity for abuse of discretion rather than *de novo*. Pet. App. 14a-15a. Applying that deferential standard, the court rejected Ebbers' claim that defense witness immunity was warranted. It found that there was no evidence that the government manipulated immunity grants "expressly for tactical reasons." Pet. App. 19a. It also found that the witnesses' testimony would not have "materially alter[ed] the total mix of evidence before the jury." Pet. App. 18a.

The court acknowledged that the proposed defense witnesses' testimony would have contradicted the government's witnesses and been inconsistent with the defense witnesses' purported out-of-court statements. *E.g.*, Pet. App. 20a, 21a, 23a. But it dismissed the proffered testimony as "self-serving" and not "credible." *E.g.*, Pet. App. 20a-24a, 23a ("[W]hile Scott's testimony would have contradicted Sullivan's, Scott's version was entirely self-serving. . . .").

The court also upheld the decision to instruct the jury on conscious avoidance, relying on circuit precedent that such an instruction is proper whenever "'(a) the element of knowledge is in dispute, and (b) the evidence would permit a rational juror to conclude beyond a reasonable doubt that the defendant was aware of a high probability of the fact in dispute and consciously avoided confirming that fact.'" Pet. App. 28a. The court found that Ebbers' attendance at meetings about line costs and revenues and his receipt of various revenue reports showed that he either knew or was aware of a high probability of fraudulent accounting. Pet. App. 29a. And it found that Ebbers' testimony—that he sometimes signed documents without reading them in full and tossed a budget report in the trash without reading it—showed that he consciously avoided knowledge of fraud. Pet. App. 30a.

REASONS TO GRANT CERTIORARI

The circuits are deeply divided on every aspect of defense witness immunity: whether a court may ever grant

immunity itself, or compel the government to grant it; whether immunity may be required where a defense witness would provide evidence crucial to the defense or only where prosecutors have engaged in serious misconduct; and whether an appellate court should review a denial of immunity *de novo* or only for abuse of discretion. The Second Circuit's rulings on these issues are among the most restrictive of all the circuits. Had Ebbers' trial been held in another circuit, his request for witness immunity would have been granted.

The circuits are also irreconcilably divided over when trial courts may give conscious avoidance instructions. Such instructions can have the effect of reducing the statutorily required *mens rea* from knowledge to negligence. On this issue, too, the Second Circuit applies the most extreme standard, allowing the instruction to be given routinely and in circumstances where other circuits would reject it.

The district court's rulings on these issues clearly affected the outcome of Ebbers' trial. They allowed the government to wield its power to grant or withhold immunity in a manner that grossly skewed the evidence, depriving Ebbers of a fair trial. And they permitted the jury to convict without having to find the *mens rea* required by statute. The Court therefore should grant certiorari "[b]ecause of the importance of the question[s] presented and the conflict of opinion on the constitutional issue[s] involved. . . ." *Fuller v. Oregon*, 417 U.S. 40, 42 (1974).

I. The Circuits Are Split On Whether And Under What Circumstances They May Require Defense Witness Immunity.

For decades, the circuits have been divided over the scope of their authority to grant or compel defense witness

immunity to protect a defendant's right to a fair trial.[9] The circuits are even more profoundly divided over *when* the Constitution may require such immunity. The Court should grant certiorari to resolve these fundamental and recurring issues.

A. The Circuits Are Divided As To Their Authority To Grant Or Compel Defense Witness Immunity

The circuits have long been divided over whether they can ever directly grant, or compel the government to grant, defense witness immunity. At one end of the spectrum, the Third Circuit has held that courts may grant "judicial immunity" to defense witnesses based on their "inherent authority" to effectuate a defendant's right to a fair trial. *Gov't of Virgin Islands v. Smith*, 615 F.2d 964, 969-70, 974 (3d Cir. 1980) ("[T]he immunity granted is a court decreed immunity; it is not achieved by any order directed to the executive, re-

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[9] The majority of circuits have held that a defendant's right to defense witness immunity is founded on the Due Process Clause of the Fifth Amendment. *See, e.g. United States v. Talley*, 164 F.3d 989, 997 (6th Cir. 1999); *United States v. Westerdahl*, 945 F.2d 1083, 1087 (9th Cir. 1991); *United States v. Angiulo*, 897 F.2d 1169, 1191-92 (1st Cir. 1990); *United States v. Hooks*, 848 F.2d 785, 799 (7th Cir. 1988); *Gov't of Virgin Islands v. Smith*, 615 F.2d 964, 970 (3d Cir. 1980). Other courts have held that the right derives from the Sixth Amendment's Compulsory Process Clause or, in certain circumstances, the Confrontation Clause. *See, e.g., United States v. Reyes*, 362 F.3d 536, 542 n.7 (8th Cir.), *cert. denied*, 542 U.S. 945 (2004); *State v. Talavera*, 243 So. 2d 595, 596-97 (Fla. 1971). Numerous commentators have also located the right at least partly in the Compulsory Process or Confrontation Clause. *See, e.g.*, Peter Westen, *The Compulsory Process Clause*, 73 Mich. L. Rev. 71, 168 (1974) ("The constitutional right of the accused to obtain immunity for his witnesses falls squarely within the language and purpose of the compulsory process clause."); John G. Douglass, *Confronting the Reluctant Accomplice*, 101 Colum. L. Rev. 1797, 1874 (2001); Note, *The Sixth Amendment Right to Have Use Immunity Granted to Defense Witnesses*, 91 Harv. L. Rev. 1266, 1271 (1978).

quiring the executive to provide statutory immunity."). *Accord United States v. Cohen*, 171 F.3d 796, 801-02 (3d Cir. 1999). The Eighth Circuit, while rejecting arguments for judicial immunity in particular cases, has stated that it might be authorized as an "'extraordinary remedy.'" *United States v. Bordeaux*, 436 F.3d 900, 905 (8th Cir. 2006) (*quoting United States v. Kehoe*, 310 F.3d 579, 591 (8th Cir. 2002)).

Most other circuits have expressly rejected the Third Circuit's theory of "judicial immunity," but have held that courts may require prosecutors either to grant statutory immunity, or face dismissal of the indictment or forego the testimony of an immunized government witness. *See, e.g., United States v. Bahadar*, 954 F.2d 821, 826 (2d Cir. 1992) ("This circuit follows the carrot-and-stick approach, leaving the immunity decision to the executive branch but interposing the judicial power to subject the government to certain choices of action."); *United States v. Burke*, 425 F.3d 400, 411 (7th Cir. 2005) ("Although a federal court cannot order the government to immunize a defense witness, courts can dismiss an indictment where the prosecutor's refusal to grant immunity has violated the defendant's right to due process."), *cert. denied*, 126 S. Ct. 2889 (2006).

At the other end of the spectrum, the District of Columbia Circuit has held that district courts lack authority to grant immunity *or* to compel the government to grant immunity, finding that immunity grants are exclusively an Executive Branch function. *See, e.g., United States v. Perkins*, 138 F.3d 421, 424 (D.C. Cir. 1998) ("[W]e have repeatedly rejected claims of judicial authority to grant such immunity."); *United States v. Lugg*, 892 F.2d 101, 104 (D.C. Cir. 1989) ("[T]he District Judge did not err in not granting immunity that he could not grant nor in not ordering the prosecution to grant immunity when he could not so order.").[10] Similarly,

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[10] *See also United States v. Heldt*, 668 F.2d 1238, 1282, 1283 (D.C.

(Continued ...)

the Fifth Circuit has noted that it has never "'upheld a grant of immunity by a trial court, and our cases have strongly suggested, without specifically deciding, that courts lack such power under any circumstances.'" *United States v. Garcia Abrego*, 141 F.3d 142, 152 (5th Cir. 1998) (citation omitted).

B. The Circuits Are Deeply Divided As To What Circumstances Require Defense Witness Immunity

Aside from the question of courts' authority to grant or compel defense witness immunity, there is an even deeper division among the circuits over the test for determining when such immunity is required to protect a defendant's right to a fair trial. The circuits have split into at least three conflicting camps, with no prospect of resolving the conflict on their own.

Three circuits have held that courts should require defense witness immunity if the witness's testimony is crucial to the defense in that it would provide exculpatory evidence, impeach the credibility of a government witness, or contradict an out-of-court statement attributed to the defense witness. Two circuits have held that courts should require such immunity if the government's selective grants of immunity have created an egregious imbalance in access to evidence. Five other circuits have rejected those approaches and held

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Cir. 1981) (stating that "[g]enerally, a trial court has no authority, in the absence of a request by the government, to provide use immunity for a defense witness," and "'it is not the proper business of the trial judge to inquire into the propriety of the prosecution's refusal to grant use immunity to a prospective witness'") (citation omitted). Although the D.C. Circuit has held open the possibility that defense immunity might be required in "'extraordinary circumstances,'" *Lugg*, 892 F.2d at 104 (citation omitted), its statements strongly suggest that it would never find defense immunity to be warranted or authorized.

that courts may not compel defense witness immunity unless there is direct evidence of serious prosecutorial misconduct. Even within these three categories, the circuits have reached widely divergent interpretations of what standard to apply to protect a defendant's constitutional right to a fair trial.

The Third, Eighth, and Ninth Circuits have held that defense witness immunity may be required if the witness's testimony is crucial to the defense—because it is exculpatory, impeaches an important government witness, or contradicts out-of-court statements introduced by the prosecution. Thus, the Third Circuit has held that "even if there is no evidence of. . .prosecutorial misconduct, when it is found that a potential defense witness can offer testimony which is clearly exculpatory and essential to the defense case and when the government has no strong interest in withholding use immunity, the court should grant judicial immunity to the witness in order to vindicate the defendant's constitutional right to a fair trial." *Smith*, 615 F.2d at 974; *accord Cohen*, 171 F.3d at 802. *See also People v. Shapiro,* 409 N.E.2d 897, 904 (N.Y. 1980) ("[I]n cases in which witnesses favorable to the prosecution are accorded immunity while those whose testimony would be exculpatory of the defendant are not, or in ones where the failure to grant immunity deprives the defendant of vital exculpatory testimony, due process may be violated.").

In a similar vein, the Ninth Circuit has held that defense witness immunity may be required where "(1) the [witness's] testimony is relevant and (2) 'the government distorted the judicial fact-finding process by denying immunity.'" *United States v. Alvarez*, 358 F.3d 1194, 1216 (9th Cir.) (*quoting United States v. Young*, 86 F.3d 944, 947 (9th Cir. 1996)), *cert. denied*, 543 U.S. 887 (2004). The Ninth Circuit has specifically held that "[t]he use of immunized testimony for the prosecution, while denying immunity to a defense witness who would directly contradict that of the government witness(es), distorts the fact-finding process." *Alvarez*, 358 F.3d at 1216 (*citing Young*, 86 F.3d at 948). Prosecutorial

threats or intimidation are not required.[11]

The Ninth Circuit has also reversed a district court's denial of a request for defense witness immunity where, as here, the witness's testimony might have impeached the credibility of a key government witness. *Young*, 86 F.3d at 948; *United States v. Westerdahl*, 945 F.2d 1083, 1087 (9th Cir. 1991). Moreover, the Ninth Circuit has held that the denial of an evidentiary hearing in such circumstances is itself reversible error. *Young*, 86 F.3d at 948-49; *Westerdahl*, 945 F.2d at 1086-87; *United States v. Lord*, 711 F.2d 887, 891-92 (9th Cir. 1983). This stands in direct conflict with the Second Circuit's rule that a prosecutor's *ex parte* affidavit forecloses any inquiry into whether defense witness immunity is constitutionally required. *See infra* pp. 17.

The Eighth Circuit has held that defense witness immunity may be granted "'where the proffered evidence is clearly exculpatory.'" *United States v. Bordeaux*, 436 F.3d 900, 905 (8th Cir. 2006); *United States v. Kehoe*, 310 F.3d 579, 591 (8th Cir. 2002). *Accord United States v. Blanche,* 149 F.3d 763, 767 (8th Cir. 1998). Moreover, in one recent case, the Eighth Circuit stated that defense witness immunity is the appropriate solution where—as here—a prosecution witness testifies as to out-of-court statements by a proposed defense witness, and the defense witness then asserts his Fifth Amendment right against self-incrimination:

> We understand the defendants' frustration in this case. The government offered Gonzalez's statements against them, but they could not call

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[11] *Westerdahl*, 945 F.2d at 1087 ("[M]isconduct is not confined solely to situations in which the government affirmatively induces a witness not to testify in favor of a defendant," but exists where the "government . . . grant[s] immunity to a witness in order to obtain his testimony, while denying immunity to a defense witness whose testimony would directly contradict that of the government witness. . . .").

> him to the stand. There is good reason to allow the Fifth Amendment [right against self-incrimination] to trump the Sixth [Amendment right to compulsory process and confrontation], but in many cases like this one the conflict between those two Amendments can be avoided by a grant of "use immunity."

United States v. Reyes, 362 F.3d 536, 542 n.7 (8th Cir. 2004) (citations omitted). *See also United States v. Paris*, 827 F.2d 395, 403 (9th Cir. 1987) (Kozinski, J., dissenting) (stating that it "amounts to a denial of due process" when a potential defense witness's out-of-court statements are admitted through a government witness but cross-examination is precluded by the prosecutor's refusal to grant immunity).

The Sixth and Seventh Circuits have rejected the "effective defense" theory, but held that courts may require defense immunity when the government's selective grants of immunity have produced "'egregiously lopsided access to evidence.'" *See, e.g., Talley*, 164 F.3d at 997 (citation omitted) ("[T]he government's selective grant of immunity to its own witnesses, while denying immunity to the defendant's witnesses, may deprive the defense of a fair trial, and in some cases require a judicially compelled immunity grant."); *id.* ("'[S]elective grants of immunity could violate due process where they produce egregiously lopsided access to evidence.'") (citation omitted); *United States v. Hooks*, 848 F.2d 785, 802-03 (7th Cir. 1988) (defense immunity may be required where "the government's selective grants of immunity have produced 'egregiously lopsided access to evidence'") (citation omitted). Thus, in those circuits, selective immunity grants by the government can justify a court's compelling the government to grant defense witness immunity, even if there is no allegation of prosecutorial misconduct or overreaching.

In direct conflict with the circuits discussed above, the Second and Fourth Circuits have held that defense witness

immunity may be compelled *only* if the defense presents direct evidence of serious prosecutorial misconduct, such as threatening or intimidating a defense witness or deliberately denying immunity to withhold exculpatory evidence and obtain a tactical advantage. *See, e.g.*, *United States v. Bahadar*, 954 F.2d 821, 826 (2d Cir. 1992) (defense immunity is appropriate only if "the government has engaged in discriminatory use of immunity to gain a tactical advantage or, through its own overreaching, has forced the witness to invoke the fifth amendment"); *United States v. Abbas*, 74 F.3d 506, 512 (4th Cir. 1996) (district court can compel immunity only when "the defendant makes a decisive showing of prosecutorial misconduct or overreaching").[12] In those circuits, the fact that the defense witness's testimony would be clearly exculpatory, directly impeach a key government witness, or contradict an out-of-court statement is insufficient to warrant immunity. Nor does it matter if the denial of immunity severely skews the evidence presented to the jury. *See, e.g.*, *Blissett v. Lefevre*, 924 F.2d 434, 442 (2d Cir. 1991) ("We have already addressed, and rejected, the argument that immunity must be granted to defense witnesses in order to redress a supposed government 'advantage' over the defense.") (citations omitted); *accord United States v. Gravely*, 840 F.2d 1156, 1160 (4th Cir. 1988).

The Fifth, Tenth, and Eleventh Circuits have left open the possibility, without deciding, that prosecutorial misconduct *may* provide a basis for defense witness immunity. But they have made clear that misconduct would be the *only* possible

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[12] The First Circuit has held that "in general, courts have no power to compel immunity in the face of a good faith refusal by the prosecutor," but has left open the possibility that immunity may be compelled "where the prosecutor has only a trivial interest in withholding immunity and . . . the defendant has an overwhelming need for specific exculpatory evidence that can be secured in no way other than through the grant of immunity." *United States v. Mackey*, 117 F.3d 24, 27 (1st Cir. 1997).

grounds. *See United States v. Garcia Abrego*, 141 F.3d 142, 152 (5th Cir. 1998) ("[T]he only situation in which due process even arguably warrants a judicial grant of immunity to a defense witness is a situation in which the government abuses its power to grant immunity to such a degree that it denies the defendant a fair trial.") (citation omitted); *United States v. Serrano*, 406 F.3d 1208, 1218 n.2 (10th Cir.) (noting that the court had "left open the question whether a district court could compel a United States attorney, on pain of dismissal, to grant immunity when the prosecutor deliberately denies immunity in an attempt to distort the fact finding process"), *cert. denied*, 126 S. Ct. 277 (2005); *accord United States v. Sawyer*, 799 F.2d 1494, 1507 (11th Cir. 1986).

Of those circuits that would consider compelling defense witness immunity only in cases of serious prosecutorial misconduct, the Second Circuit goes even further, virtually foreclosing any possibility of such immunity. It instructs district courts to "summarily reject claims for defense witness immunity" whenever the prosecutor presents "*in camera* an *ex parte* affidavit" declaring that the witness is "an actual or potential target of prosecution," and that "[n]o hearing should be held to establish such status." *United States v. Turkish*, 623 F.2d 769, 778 (2d Cir. 1980). This standard allows the government to completely preclude testimony from a crucial defense witness merely by stating that the witness is a *potential* target of investigation. The conflict between the Second Circuit and other circuits could not be more stark.[13]

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[13] As noted above, the Ninth Circuit deems it reversible error if the district court refuses to hold a hearing to consider a defendant's claim that the denial of immunity distorts the fact-finding process. Even circuits that require a showing of prosecutorial misconduct have similarly held that it is reversible error to refuse to hold an evidentiary hearing. *See, e.g.*, *United States v. Schlei*, 122 F.3d 944, 992 (11th Cir. 1997).

C. Other Circuits' Standards Would Have Produced A Different Result In This Case

Had the government prosecuted Ebbers in another circuit, his request for defense witness immunity would have been granted. The Second Circuit acknowledged that the proffered testimony would have contradicted the government's key witnesses, and that Ebbers' witnesses would have denied making statements attributed to them by the government's witnesses. *See supra* pp. 8. Ebbers thus would have satisfied the standards for defense witness immunity in the Ninth and Eighth Circuits. At the very least, the Ninth Circuit would have required a hearing to assess Ebbers' need for the evidence and the government's interest in withholding immunity for witnesses whom the government—*to this day*—has never charged with a crime.

Courts in the Third Circuit also would have required immunity for Ebbers' proposed witnesses. As discussed above, *supra* pp. 7, the government featured two out-of-court statements by Ebbers' witnesses as among the "Top Ten" most incriminating items of evidence. Tr. 4242-43. Had those witnesses been immunized, they would have contradicted those statements. Pet. App. 20a, 21a, 23a. By any reasonable definition, evidence that would directly refute two of the government's principal pieces of evidence and undermine the government's theory of a criminal conspiracy is evidence necessary to an "effective defense." *Cf. Washington v. Texas*, 388 U.S. 14, 19 (1967) ("The right to offer the testimony of witnesses . . . is in plain terms the right to present a defense, the right to present the defendant's version of the facts as well as the prosecution's to the jury so it may decide where the truth lies."); *Cool v. United States*, 409 U.S. 100, 104 (1972) (per curiam) ("[A] criminal defendant has a Sixth Amendment right to present to the jury exculpatory testimony of an accomplice.").

The government's selective grants of immunity also met

the standard of the Sixth and Seventh Circuits for compelling defense witness immunity. The government's case was built on the testimony of eight immunized prosecution witnesses. Yet the government denied immunity to *all* the defense witnesses who would have contradicted the government's witnesses on issues that the prosecution deemed crucial to its case. The government's selective use of immunity thus created an "egregious imbalance" in access to evidence.[14]

II. The Circuits Are Divided on The Standard of Review For Decisions On Defense Witness Immunity.

As the Second Circuit acknowledged below, Pet. App. 14a, the circuits are split on what standard of review to apply to decisions on for defense witness immunity. The Fourth and Ninth Circuits review such decisions *de novo*, treating the issue as a mixed question of law and fact. *See United States v. Washington*, 398 F.3d 306, 310 (4th Cir.), *cert. denied*, 545 U.S. 1109 (2005); *Alvarez*, 358 F.3d at 1216.

Four other circuits, including the Second Circuit, apply an abuse of discretion standard. Pet. App. 14a-15a; *United States v. Perez*, 280 F.3d 318, 348 (3d Cir. 2002); *United States v. Burke*, 425 F.3d 400, 411 (7th Cir. 2005), *cert. denied*, 126 S. Ct. 2889 (2006); *United States v. Doddington*, 822 F.2d 818, 821 (8th Cir. 1987). The Tenth Circuit has applied both standards in recent years. *United States v. Apperson*, 441 F.3d 1162, 1203 (10th Cir. 2006) (abuse of discretion); *Serrano*, 406 F.3d at 1214 (*de novo*).

The abuse of discretion standard conflicts with this Court's decisions on analogous issues. A district court's pure findings of fact may appropriately be reviewed under a

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[14] That imbalance was compounded by the district court's denial of Ebbers' motions to impeach the co-conspirator statements with prior inconsistent statements or to have the court give a missing witness instruction. *See supra* pp. 6.

deferential abuse of discretion standard. But the question of whether defense witness immunity is warranted in a particular case involves the application of constitutional requirements to specific facts. Such mixed questions of law and fact must be reviewed *de novo* so that appellate courts can ensure a consistent interpretation of constitutional principles. *See Ornelas v. United States*, 517 U.S. 690, 697, 699 (1996) ("determinations of reasonable suspicion and probable cause should be reviewed *de novo*" so that appellate courts can "maintain control of, and . . . clarify, the legal principles"); *Cooper Indus., Inc. v. Leatherman Tool Group, Inc.*, 532 U.S. 424, 436 (2001) ("[C]ourts of appeals should apply a *de novo* standard of review when passing on district courts' determinations of the constitutionality of punitive damages awards."); *Thompson v. Keohane*, 516 U.S. 99, 111, 113 (1995) (appellate courts should review *de novo* whether a suspect was in custody for *Miranda* purposes, since that issue "presents a 'mixed question of law and fact' qualifying for independent review"); *Miller v. Fenton*, 474 U.S. 104, 112 (1985) ("[T]he ultimate question whether, under the totality of the circumstances, the challenged confession was obtained in a manner compatible with the requirements of the Constitution is a matter for independent federal determination."). This Court should grant certiorari to resolve this split.

III. The Circuits Are Divided Over When Trial Courts May Give A Conscious Avoidance Jury Instruction.

The circuits have long been divided over when trial courts may give a conscious avoidance instruction.[15] Indeed, the United States fourteen years ago urged the Court to grant

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[15] Courts also use terms such as "willful blindness," "deliberate blindness," "deliberate ignorance," "deliberate indifference," and "deliberate avoidance" to refer to the same concept. Because the Second Circuit used the term "conscious avoidance" below, we use that term throughout this petition, except where quoting a court's own usage.

certiorari to resolve a split among the circuits on this issue. *See* Br. of United States at 10, 12, 14 (*Tomala v. United States*, No. 91-7051) (Mar. 25, 1992) ("[T]h circuits are in conflict concerning whether an instruction such as the one given in this case properly defines 'knowledge' for purposes of the criminal law and thus can properly be given whenever knowledge is an issue in a criminal case. Since the issue arises quite frequently, further review by this Court to resolve the conflict is warranted."). The reasons for granting certiorari are even more evident today, with courts continuing to apply different standards.[16]

A conscious avoidance instruction should never be permitted where a criminal statute requires a jury to find that the defendant acted knowingly. As Judge Easterbrook has noted, "Knowledge in a criminal statute means *actual* knowledge. What one ought to have known, but did not know, is not knowledge; it is not even (necessarily) recklessness." *United States v. Ladish Malting Co.*, 135 F.3d 484, 488 (7th Cir. 1998) (citation omitted); *see also United States v. Alston-Graves*, 435 F.3d 331, 337 (D.C. Cir. 2006) (Randolph, J.) ("It makes obvious sense to say that a person cannot act 'knowingly' if she does not know what is going on. To add that such a person nevertheless acts 'knowingly' if she intentionally does not know what is going on is something else again."); *United States v. Jewell*, 532 F.2d 697, 706 (9th Cir. 1976) (en banc) (Kennedy, J., dissenting) ("When a statute specifically requires knowledge as an element of a crime, . . . the substitution of some other state of mind cannot be justified even if the court deems that both are equally blameworthy."). When a court allows a jury to convict on the basis of the defendant's conscious avoidance of actual knowledge, it

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[16] Indeed, the United States in its brief to the Second Circuit in this case acknowledged that "Ninth Circuit law . . . is plainly inconsistent with Second Circuit law." Gov't Br. at 81 n*.

effectively replaces the *mens rea* required by Congress—knowledge—with a lesser standard,[17] raising serious separation of powers and due process problems.[18] This conclusion is buttressed by the fact that when Congress wants to criminalize conscious avoidance or some other mental state short of actual knowledge, it knows how to do so.[19]

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[17] *United States v. Rivera*, 944 F.2d 1563, 1571 n.30 (11th Cir. 1991) ("deliberate ignorance is easier to prove than actual knowledge").

[18] *See Dowling v. United States*, 473 U.S. 207, 214 (1985) ("'It is the legislature, not the Court, which is to define a crime. . . .'") (*quoting United States v. Wiltberger*, 18 U.S. (5 Wheat.) 76, 95 (1820) (Marshall, C.J.)); *Morissette v. United States*, 342 U.S. 246, 263 (1952) ("The spirit of the doctrine which denies to the federal judiciary power to create crimes forthrightly admonishes that we should not enlarge the reach of enacted crimes by constituting them from anything less than the incriminating components contemplated by the words used in the statute."); *Sandstrom v. Montana*, 442 U.S. 510, 521 (1979) ("[A] jury instruction [that] had the effect of relieving the State of the burden of proof . . . on the critical question of petitioner's state of mind . . . represents constitutional error."); *In re Winship*, 397 U.S. 358, 364 (1970) ("[T]he Due Process Clause protects the accused against conviction except upon proof beyond a reasonable doubt of every fact necessary to constitute the crime with which he is charged.").

[19] *See, e.g.*, 31 U.S.C. § 3729(b) (a person acts "knowingly" for purposes of False Claims Act when he "has actual knowledge," "acts in deliberate ignorance," or "acts in reckless disregard of" the "truth or falsity of the information"); 18 U.S.C. § 2424(a) (criminalizing the harboring of persons for illicit purposes while "knowing or in reckless disregard of the fact" that they are aliens); *id.* § 175b(b) (criminalizing transfer of biological agents where transferor "knows or has reasonable cause to believe" that the agents are being delivered to unlicensed persons); *id.* § 792 (criminalizing the harboring of a person one "knows, or has reasonable grounds to believe or suspect," is about to commit espionage); *id.* § 842(h) (penalizing receipt of explosives by one "knowing or having reasonable cause to believe" they were stolen); *id.* § 2332d(a) (penalizing those who do business with a foreign nation "knowing or having reasonable cause to know" that the nation sponsors terrorism); *id.* § 2339(a) (penalizing harboring of persons who one "knows, or has reasonable grounds to believe" have or will commit terrorist acts); 21 U.S.C. §

(Continued ...)

If a conscious avoidance instruction can *ever* be appropriate where the statute requires the jury to find knowledge, the Court should grant certiorari to resolve a split over when such an instruction is permitted. The circuits are so widely split on this issue that whether a defendant is convicted or acquitted can depend on the circuit in which he is prosecuted.[20]

Most circuits have stressed that the instruction should "rarely" be given because of the risk that even a properly worded instruction will confuse the jury and allow it to convict on a negligence theory. *See, e.g.*, *United States v. Mendoza-Medina*, 346 F.3d 121, 132 (5th Cir. 2003) ("'Because the instruction permits a jury to convict a defendant without a finding that the defendant was actually aware of the existence of illegal conduct, the deliberate ignorance instruction poses the risk that a jury might convict the defendant on a lesser negligence standard—the defendant should have been aware of the illegal conduct.'") (citation omitted), *cert. denied*, 540 U.S. 1156 (2004); *id.* at 134 ("We have repeatedly stated that the instruction should rarely be given because it possesses a danger of confusing the jury."); *United States v. Barnhart*, 979 F.2d 647, 651 (8th Cir. 1992) ("[D]espite the instruction's cautionary disclaimer, there is a possibility that the jury will be led to employ a negligence standard and convict a defendant on the impermissible ground that he should have known [an illegal act] was taking place.") (citation omitted)

321(bb)(2) (defining "knowingly" for purpose of Food, Drug, and Cosmetic Act as including "acts in deliberate ignorance or reckless disregard of the truth or falsity of the information"); *id.* § 843(a)(6), (7) (penalizing possession, manufacture, sale, import, or export of devices while "knowing, intending, or having reasonable cause to believe" that they will be used to manufacture illicit drugs); 19 U.S.C. § 1594(b)(2).

[20] *See Alston-Graves*, 435 F.3d at 337 (noting that circuits differ on their "rationales" for the doctrine, "limits on the doctrine's proper use, and "wording of the instructions").

(alteration in original). *See also United States v. Murrieta-Bejarano*, 552 F.2d 1323, 1326 (9th Cir. 1977) (Kennedy, J., concurring in part and dissenting in part) ("The danger is that juries will avoid questions of scienter and convict under the standards analogous to negligence. Such convictions are wholly inconsistent with the statutory requirement of scienter."); *United States v. Jewell*, 532 F.2d 697, 707 (9th Cir. 1976) (en banc) (Kennedy, J., dissenting) ("The failure to emphasize . . . that subjective belief is the determinative factor[] may allow a jury to convict on an objective theory of knowledge—that a reasonable man should have inspected the car and would have discovered what was hidden inside.").[21]

In acknowledged conflict with other circuits, the Second Circuit authorizes the instruction "more readily than elsewhere," and "commonly use[s]" it. *United States v. Rodriguez*, 983 F.2d 455, 457 (2d Cir. 1993); *accord United States v. Mang Sun Wong*, 884 F.2d 1537, 1543 n.5 (2d Cir. 1989) ("[t]he Second and Ninth Circuits arguably have different views concerning use of the 'conscious avoidance' charge," with the instruction "commonly . . . used" in the Second but "rare[ly]" in the Ninth); *United States v. Reyes*, 302 F.3d 48, 55 (2d Cir. 2002) (instruction "commonly given").

Moreover, the circuits are split over the standard for determining whether the instruction should be given. The Second Circuit permits the instruction whenever a defendant disputes knowledge of a material fact and there is evidence to support an inference that "the defendant (1) was aware of a high probability of the disputed fact and (2) deliberately

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[21] *See also United States v. Hanzlicek*, 187 F.3d 1228, 1233 (10th Cir. 1999) ("instruction 'is rarely appropriate'") (citation omitted). *Accord United States v. Carrillo*, 435 F.3d 767, 781 (7th Cir.), *cert. denied*, 126 S. Ct. 2344 (2006); *United States v. Prather*, 205 F.3d 1265, 1270 (11th Cir. 2000); *United States v. Ruhe*, 191 F.3d 376, 385 (4th Cir. 1999); *United States v. Littlefield*, 840 F.2d 143, 148 (1st Cir. 1988).

avoided confirming that fact." *United States v. Svoboda*, 347 F.3d 471, 480 (2d Cir. 2003), *cert. denied*, 541 U.S. 1044 (2004). Several circuits employ a similar test. *See United States v. Flores*, 454 F.3d 149, 155 (3d Cir. 2006); *United States v. Guay*, 108 F.3d 545, 551 (4th Cir. 1997); *United States v. Lara-Velasquez*, 919 F.2d 946, 952 (5th Cir. 1990); *United States v. Lee*, 991 F.2d 343, 350 (6th Cir. 1993); *United States v. Carrillo*, 435 F.3d 767, 780 (7th Cir. 2006).

The Second Circuit has loosened this standard further, holding that "'[a] defendant's involvement in the criminal offense may have been so overwhelmingly suspicious that the defendant's failure to question the suspicious circumstances establishes the defendant's purposeful contrivance to avoid guilty knowledge.'" *Svoboda*, 347 F.3d at 480 (*quoting Lara-Velasquez*, 919 F.2d at 952). This was the standard applied by the district court below. Pet. App. 49a, 107a.

Other circuits reject the notion that failure to investigate suspicious circumstances is enough to establish conscious avoidance. Moreover, they add a third prong to the test, permitting the instruction only where the evidence shows that the defendant: "(1) actually suspected that he or she might be involved in criminal activity, (2) deliberately avoided taking steps to confirm or deny those suspicions, and (3) did so *in order to provide himself or herself with a defense in the event of prosecution.*" *United States v. Baron*, 94 F.3d 1312, 1318 n.3 (9th Cir. 1996) (emphasis added).

This has long been the standard in the Ninth Circuit. As then-Judge (now Justice) Kennedy wrote for that court in reversing a conviction under the Toxic Substances Control Act:

> [T]he government must present evidence indicating that defendant purposely contrived to avoid learning all of the facts in order to have a defense in the event of subsequent prosecution. Absent such evidence, the jury might impermissibly infer guilty knowledge on the basis of

> mere negligence without proof of deliberate avoidance. . . . In the case before us, the government has presented insufficient evidence of willful blindness on the part of defendants to warrant a [deliberate avoidance] instruction. There was no evidence that defendants deliberately avoided learning the true nature of the fluid inside the capacitors so as to build a defense in the event of arrest.

United States v. Pac. Hide & Fur Depot, Inc., 768 F.2d 1096, 1098-99 (9th Cir. 1985) (citation omitted)). *See also Murrieta-Bejarano*, 552 F.2d at 1325 (Kennedy, J., concurring in part and dissenting in part) ("The prosecution offered no proof, either in its case in chief or on rebuttal, that would show that the defendant, in order to concoct a defense to potential criminal charges, deliberately chose to avoid learning about the contraband.").[22]

The First, Eighth, Tenth, and Eleventh Circuits have applied a similar test. *See, e.g., United States v. Bilis*, 170 F.3d 88, 92 (1st Cir. 1999) ("[A] willful blindness instruction is proper when there is evidence to 'support the inference that defendant was aware of a high probability of the existence of the fact in question and purposely contrived to avoid learning all of the facts in order to have a defense in the event of a subsequent prosecution.'") (citation omitted). *Accord United States v. Brandon*, 17 F.3d 409, 452 (1st Cir. 1994); *United*

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[22] Applying this standard, the Ninth Circuit has repeatedly reversed convictions where the district court erroneously gave an instruction on deliberate ignorance. *United States v. Aguilar*, 80 F.3d 329, 333 (9th Cir. 1996) (en banc); *United States v. Mapelli*, 971 F.2d 284, 286-87 (9th Cir. 1992); *United States v. Sanchez-Robles*, 927 F.2d 1070, 1075-76 (9th Cir. 1991); *United States v. Beckett*, 724 F.2d 855, 856 (9th Cir. 1984); *United States v. Garzon*, 688 F.2d 607, 609 (9th Cir. 1982). *See also United States v. Heredia*, 429 F.3d 820, 824 (2005), *vacated upon grant of rehearing en banc*, 460 F.3d 1093 (9th Cir. 2006).

States v. Barnhart, 979 F.2d 647, 652 (8th Cir. 1992); *United States v. Willis*, 277 F.3d 1026, 1032 (8th Cir. 2002); *United States v. Soussi*, 316 F.3d 1095, 1106-07 (10th Cir. 2002); *United States v. Puche*, 350 F.3d 1137, 1149 & n.6 (11th Cir. 2003); *United States v. Rivera*, 944 F.2d 1563, 1571 (11th Cir. 1991). The Fourth Circuit, however, has expressly rejected this test. *See, e.g., United States v. Ruhe*, 191 F.3d 376, 385 (4th Cir. 1999) ("[T]his circuit has never adopted the Ninth Circuit's additional requirement that the government prove that the defendant's ignorance was for the purpose of providing a defense in case of prosecution.").

Courts are also split on whether it is appropriate to give the instruction where the government's case is based primarily on a theory of actual knowledge. Once again, the Second Circuit has adopted the most extreme approach, holding that a conscious avoidance instruction "is not inappropriate merely because the government has primarily attempted to prove that the defendant had actual knowledge, while urging in the alternative that if the defendant lacked such knowledge it was only because he had studiously sought to avoid knowing what was plain." *United States v. Hopkins*, 53 F.3d 533, 542 (2d Cir. 1995). The Second Circuit also allows the government to rely on the same evidence to infer both actual knowledge and conscious avoidance. *See Svoboda*, 347 F.3d at 480 ("'[T]he same evidence that will raise an inference that the defendant had actual knowledge of the illegal conduct ordinarily will also raise the inference that the defendant was subjectively aware of a high probability of the existence of illegal conduct.'") (citation omitted). The Fifth Circuit applies the same rule. *See United States v. Freeman*, 434 F.3d 369, 378-79 (5th Cir. 2005).

Other circuits have rejected the Second Circuit's approach. The Ninth Circuit has held that a conscious avoidance instruction "is not appropriate where the only evidence alerting a defendant to the high probability of criminal activity is direct evidence of the illegality itself." *Sanchez-Robles*,

927 F.2d at 1074. Thus, the government cannot rely on the same evidence to show both actual knowledge and conscious avoidance. *Id.* Indeed, the Ninth Circuit has repeatedly reversed convictions on this precise ground.[23]

Similarly, the First Circuit allows the instruction only if "'*separate and distinct* evidence supports a defendant's deliberate avoidance of knowledge. . . .'" *United States v. Bilis*, 170 F.3d 88, 93 (1st Cir. 1999) (emphasis added) (*quoting United States v. Brandon*, 17 F.3d 409, 452 n.74 (1st Cir. 1994)). The Tenth Circuit has also held that "the same evidence cannot be used as proof for the mutually exclusive categories of actual knowledge of an operant fact and deliberate ignorance of that same fact" and "the deliberate ignorance instruction must not be tendered to the jury unless sufficient independent evidence of deliberate avoidance of knowledge has been admitted." *United States v. de Francisco-Lopez*, 939 F.2d 1405, 1410 (10th Cir. 1991); *id.* ("We emphasize, the same fact or facts cannot be used to prove both actual knowledge *and* deliberate indifference because the two are mutually exclusive concepts. If evidence proves the defendant actually *knew* an operant fact, the same evidence could not *also* prove he was *ignorant* of that fact.").[24]

This court should grant certiorari to resolve these splits among the circuits.[25] The Second Circuit's "suspicious cir-

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[23] *Sanchez-Robles*, 927 F.2d at 1079; *Pac. Hide & Fur Depot, Inc.*, 768 F.2d at 1099; *United States v. Beckett*, 724 F.2d 855, 856 (9th Cir. 1984); *United States v. Garzon*, 688 F.2d 607, 609 (9th Cir. 1982).

[24] A subsequent panel of the Tenth Circuit declined to follow that portion of the ruling in *de Francisco-Lopez*, see *United States v. Espinoza*, 244 F.3d 1234, 1244 (10th Cir. 2001), thus apparently leaving the issue unresolved in that circuit.

[25] The circuits are also split over the appropriate standard of review to apply to decisions regarding conscious avoidance instructions. The Second, Third, Ninth, and Tenth Circuits review those decisions *de novo*. *See* Pet. App. 28a; *United States v. Aina-Marshall*, 336 F.3d 167, 170 (2d

(Continued ...)

cumstances" test raises serious due process and separation of powers problems, as it shifts the focus from a defendant's subjective state of mind—her awareness of possible illegal activity, and her deliberate effort to avoid confirming it—to the nature of the activity and whether a reasonable person should have known something was amiss. *Cf. Arthur Anderson LLP v. United States*, 544 U.S. 696, 706 (2005) (reversing conviction because jury instruction on obstruction of justice "failed to convey the requisite consciousness of wrongdoing") (citation omitted).

This case presents an appropriate vehicle for resolving these splits because courts in other circuits would not have given a conscious avoidance instruction if Ebbers' trial had been held there. First, there was no evidence that Ebbers consciously avoided confirming the existence of fraud for the purpose of creating a defense in the event of prosecution. Second, the government's case was built on the theory that Ebbers had actual knowledge of, and directed, fraud at WorldCom. Third, the courts below cited the same evidence as showing "that Ebbers actually knew or was aware of the

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Cir. 2003); *United States v. Stewart*, 185 F.3d 112,126 (3d Cir. 1999); *United States v. Wert-Ruiz*, 228 F.3d 250, 255 (3d Cir. 2000); *United States v. Shannon*, 137 F.3d 1112, 1117 (9th Cir. 1998); *United States v. Soussi*, 316 F.3d 1095, 1106-07 (10th Cir. 2002); *Espinoza*, 244 F.3d at 1241. The Fourth, Fifth, Sixth, Seventh, and Eighth Circuits review only for abuse of discretion. *United States v. Ruhe*, 191 F.3d 376, 385 (4th Cir. 1999); *United States v. Freeman*, 434 F.3d 369, 377 (5th Cir. 2005); *United States v. Carney*, 387 F.3d 436, 448-49 (6th Cir. 2004); *United States v. Beaty*, 245 F.3d 617, 621 (6th Cir. 2001); *United States v. Carrillo*, 435 F.3d 767, 780 (7th Cir.), *cert. denied*, 126 S. Ct. 2344 (2006); *United States v. Florez*, 368 F.3d 1042, 1044 (8th Cir. 2004). The First Circuit recently acknowledged a split in the circuits, and inconsistency within the First Circuit itself, but did not decide the appropriate standard. *United States v. Epstein*, 426 F.3d 431, 440 n.5 (1st Cir. 2005) ("The parties argue about whether review on this issue should be *de novo* or abuse of discretion. Varying language appears in our own cases and in decisions of the circuits."), *cert. denied*, 126 S. Ct. 1596 (2006).

high probability that the financial statements were false." Pet. App. 29a. And as the government itself acknowledged at trial, the conscious avoidance instruction may have been critical to the jury's verdict, since it was possible the jury "could not believe Mr. Sullivan" and therefore not find actual knowledge, but "could also not believe everything Mr. Ebbers said" and so convict on the basis "that he consciously avoided reacting to what was right before him." J.A. 364. "[T]he outcome of a federal criminal prosecution should not depend upon the circuit in which the case is tried." *Tomala v. United States*, 504 U.S. 932, 933 (1992) (White, J., joined by Thomas, J., dissenting from denial of certiorari on conscious avoidance issue).

CONCLUSION

For the foregoing reasons, the Court should grant this Petition.

Respectfully submitted,

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October 26, 2006

APPENDIX

APPENDIX A — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT DECIDED JULY 28, 2006

UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

August Term, 2005

(Argued: January 30, 2006 Decided: July 28, 2006)

Docket No. 05-4059-cr

UNITED STATES OF AMERICA,

Appellee,

v.

BERNARD J. EBBERS,

Defendant-Appellant.

Before: WINTER, CABRANES, and B.D. PARKER, *Circuit Judges.*

WINTER, *Circuit Judge*:

Bernard J. Ebbers appeals from his conviction by a jury on nine counts of conspiracy, securities fraud, and related crimes and from the 25-year jail sentence imposed by Judge Jones.

Appendix A

Ebbers was the Chief Executive Officer ("CEO") of WorldCom, Inc., a publicly traded global telecommunications company. During the pertinent times — from the close of the fourth quarter of the 2000 fiscal year through the first quarter of the 2002 fiscal year — he engineered a scheme to disguise WorldCom's declining operating performance by falsifying its financial reports. Although the scheme was multi-faceted, the fraud primarily involved the treating of hundreds of millions of dollars of what had always been recorded operating costs as capital expenditures for several fiscal quarters. After a seven week trial, the jury convicted Ebbers on all counts. He was sentenced to 25 years' imprisonment, to be followed by 3 years' supervised release.

On appeal, Ebbers principally contends that the district court erred in permitting the government to introduce testimony by immunized witnesses while denying immunity to potential defense witnesses who were rendered unavailable to Ebbers by their invocation of the privilege against self-incrimination. He also claims that the court should not have given a conscious avoidance instruction and that the government should have been required to allege and prove violations of Generally Accepted Accounting Principles ("GAAP"). Finally, he challenges his sentence as based on an inaccurate calculation of losses to investors, as significantly greater than those imposed on his co-conspirators, and as unreasonable in length. We affirm.

Appendix A

BACKGROUND

We must of course view the evidence in the light most favorable to the government and draw all permissible inferences from that evidence in its favor. *Glasser v. United States*, 315 U.S. 60, 80, 62 S.Ct. 457, 86 L.Ed. 680 (1942).

a) *Beginnings*

There is an element of tragedy here in that it was not a lack of legitimate entrepreneurial skills that caused Ebbers to resort to fraud. Before WorldCom, he was, among other things, a teacher, coach, and warehouse manager. He was a motel operator when, in 1983, he first invested in Long Distance Discount Services ("LDDS"), a small long distance company in Mississippi. When LDDS was in danger of failing in 1985, Ebbers agreed to become its CEO and led it to profitability by merging with other long distance providers. In 1989, LDDS went public by merging with Advantage Companies, another telecommunications company that was listed on NASDAQ. In 1995, LDDS changed its name to WorldCom, Inc. After WorldCom acquired MCI, Inc., in 1998, it was a global company with subsidiaries in Brazil, Mexico, and Canada. WorldCom then tried to acquire Sprint, but the Justice Department and the European Union stopped the merger on antitrust grounds. Having exhausted the market for acquisition targets in the long distance business, WorldCom began to acquire web hosting services. By 2000, WorldCom had about 90,000 employees in 65 countries, and reported revenues of $39 billion.

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As part of its business, WorldCom built a global network of fiber-optic cables and telephone wires to transmit data and telephone calls. It also leased capacity on other companies' network facilities to transmit data and calls. The cost of the leasing was WorldCom's single largest expense — styled "line costs." When the "dot-com bubble" burst in early 2000, WorldCom's business slowed dramatically as some of its dot-com customers were unable to pay their bills and demand for WorldCom's internet services declined. Anticipating growth rather than declining demand, WorldCom had added 10,000 new employees, continued to invest heavily in new equipment, and had taken on long-term line leases with fixed monthly payments. By the end of the third quarter of 2000, as its revenue growth decreased and its expenses increased, the company could no longer meet investors' expectations of revenue and profit growth.

b) *Ebbers' Personal Finances*

By this time, Ebbers had powerful personal as well as occupational motives to see that investors' expectations were met and that WorldCom's stock price did not fall. Although Ebbers had become very wealthy since his earlier days, his consumption and investment habits outpaced his income. Ebbers had accumulated millions of shares of WorldCom stock but had borrowed over $400 million from banks, using his stock in WorldCom as collateral. As WorldCom's stock price began to drop in 2000, Ebbers received margin calls from the banks, requiring him either to put up more stock as collateral or to pay back a portion of the money he owed. Because he had used much of the borrowed money to buy relatively illiquid assets, such as a ranch, timber lands, and a

yacht-building company, Ebbers could not use those assets to meet the margin calls. As WorldCom's stock price continued to fall, Ebbers pledged more of his WorldCom stock until every share he owned was collateral for the loans. By October 2000, Ebbers entered into a forward sale transaction, allowing Bank of America to sell some of his WorldCom stock at a future date in exchange for $70.5 million in cash to pay off his margin debts. WorldCom assumed the liability for the debts to the banks in October 2000, requiring Ebbers to make payments directly to WorldCom in the amount the company owed the banks; the debts to WorldCom and to the banks were still secured by Ebbers' WorldCom stock.

c) *Third Quarter 2000*

As a public company, WorldCom was required to file quarterly financial statements and annual reports with the SEC. When it became clear that the company would be unable to meet analysts' expectations in the third quarter of 2000, Ebbers and WorldCom's Chief Financial Officer ("CFO") Scott Sullivan reviewed the monthly revenue reports and discussed the company's options. Sullivan told Ebbers that WorldCom's financial performance had deteriorated and that they should issue an earnings warning to investors. Ebbers refused. Sullivan then told Ebbers that to meet expectations the company would have to make an improper adjustment to the revenue figure. Ebbers replied that "[W]e have to hit our numbers." Sullivan instructed others to increase the publicly reported revenues by adding $133 million in anticipated under-usage penalties to the revenue calculation, even though he believed that those penalties were not likely to be collected.

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Soon after, Sullivan learned that line cost expenses would be almost $1 billion greater than expected. He reported that to Ebbers, who reiterated that the company had to hit its quarterly earnings estimates. Sullivan instructed Controller David Myers and his subordinates Buford Yates, Betty Vinson, and Troy Normand to reduce line cost expense accounts in the general ledger while also reducing reserves in the same amounts, which lowered the reported line costs by about $828 million. As a result, WorldCom's reported earnings were increased by the same amount.

Vinson and Normand believed the entries were wrong and considered resigning. When Sullivan told Ebbers that the accounting staff might quit, Ebbers told Sullivan that "we shouldn't be making adjustments; we've got to get the operations of this company going; we shouldn't be putting people in this position." Ebbers then spoke to Controller Myers, apologizing for the position that Myers and his staff were put in. In November 2000, WorldCom lowered its future earnings estimates and offered new guidance to analysts.

d) *Fourth Quarter 2000*

WorldCom's revenues and line costs did not improve in the fourth quarter of 2000. In January 2001, Ebbers and Sullivan agreed that WorldCom would not be able to meet even the analysts' revised expectations if it reported its actual results. Sullivan asked Ebbers if he would again reduce the earnings estimate given to analysts, but Ebbers refused to do so. Sullivan asked Myers to alter the reported revenue and expense numbers to meet expectations. The commissions paid to airlines as part of a marketing partnership were no

longer removed from the reported revenues, increasing the revenue reported by about $42 million.

WorldCom's line cost expenses were $800 million above analysts' expectations. Sullivan directed Myers to bring the reported line costs in line with expectations. Myers and his staff then reduced the income tax reserve by $407 million, and altered other accounts until they were able to reduce the reported line costs by $797 million for the fourth quarter. Monthly reports sent to Ebbers, referred to at trial as the Monthly Budget Variation Reports ("MBVRs"), detailed the company's financial results and included the reduced line costs, giving the company an apparent gross margin of 78% in September 2000 and 74% in December 2000 — margins that had never been achieved by WorldCom before. The 2000 annual report and Form 10-K also contained the false information.

e) *First Quarter 2001*

In early 2001, WorldCom's line costs were still hundreds of millions of dollars higher than the company had predicted, again making it impossible to meet analysts' expectations without further manipulation of the company's financial reports. The staff had been asked to find ways to reduce line costs, but the proposed cost savings were far smaller than needed to meet expectations. When the first quarter ended, reserves had been largely exhausted and could no longer be used to reduce line costs. Sullivan suggested capitalization of the line costs, that is, shifting a portion of the costs out of reported current expenses into capital expenses. Because line costs had always been treated as operating expenses, their

unannounced treatment as capital expenses would disguise the decline in earnings. Myers and his staff agreed to capitalize about $771 million in line costs, although they believed it to be improper. At a dinner in Washington in March 2001, Sullivan and Ebbers discussed the line cost problem. Sullivan told Ebbers that the planned allocation of current expenses to capital expenses — in an amount over $500 million — "wasn't right." Ebbers did not deter him from the allocation.

Ebbers approved the capitalization of line costs in a later conversation with Sullivan. He told Sullivan that "[w]e have to grow our revenue and we have to cut our expenses, but we have to hit the numbers this quarter." Sullivan told Myers to change the general ledger to capitalize a portion of the line cost expenses in an amount totaling hundreds of millions of dollars. Ebbers later told Sullivan to change the format of the reports to remove the line cost figures. When Ebbers spoke to analysts and the public about WorldCom's first quarter performance in the earnings conference call, he did not mention the change in how the company was booking line costs. Instead, he said "there were no storms on the horizon," urging them to "go out and buy stock."

f) *Second Quarter 2001*

Capitalizing WorldCom's line cost expenses left another problem unaddressed: revenues were not growing at the 12% annual rate that Ebbers had predicted. Missing the revenue growth target was likely to lower WorldCom's stock price. Sullivan, Ebbers, and a handful of other executives created a new program called "Close the Gap" to "get [the] operating

performance ... up to the market guidance expectations" by finding new items to include in revenue. Each month, and sometimes more often, the business operations group presented revenue data to Ebbers in detail as part of the "Close the Gap" program. Sullivan told Ebbers that there was no basis for including many of the opportunities presented in the "Close the Gap" program in reported revenues. In a voicemail to Ebbers, Sullivan described some of the items eventually included in reported revenues as "accounting fluff," "one-time stuff," and "junk." In July 2001, Ebbers sent a memorandum to Chief Operating Officer ("COO") Ron Beaumont, who was involved in the "Close the Gap" program, asking him "[w]here we stand on those one time events that had to happen in order for us to have a chance to make our numbers." Ebbers and Sullivan were aware that the company's true results fell far short of analysts' expectations, but ordered the improper revenue accounting so that those expectations would be met.

Once again, Sullivan told Ebbers that the company could reach the analysts' estimates only by capitalizing a portion of its line costs. Ebbers attended one of the line cost meetings around this time, and explained to the employees there that his "lifeblood was in the stock of the company" and that if the price fell below about $12 per share, he would be wiped out financially by margin calls. Although the line costs had improved slightly since the previous quarter, the accounting staff still had to capitalize over $610 million in line costs in order to meet earnings estimates.

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g) *Third Quarter 2001*

In the third quarter of 2001, WorldCom's actual revenue growth rate, as reported internally to Ebbers, had fallen to about 5.5%. However, Ebbers announced that WorldCom had sustained its 12% revenue growth rate when the third quarter results were reported. The "Close the Gap" program added several new revenue items, largely one-time items not previously counted in revenue. Sullivan told Ebbers that the purpose of the adjustments to revenue was to reach the 12% growth target. WorldCom's press release announcing the quarterly results quoted Ebbers as saying the company had "delivered excellent growth this quarter." During the earnings conference call with analysts, Ebbers said "[w]e were able to achieve very solid growth." However, over $700 million in line costs had to be capitalized to create the appearance of meeting the earnings target for the quarter.

At the time, WorldCom was in merger negotiations with Verizon. Concerned that Verizon might discover the capitalization of line costs and the revenue adjustments in the course of a due diligence inquiry, Ebbers abruptly ended the merger negotiations.

At the board meeting in June 2001, board members began to ask about the "Close the Gap" program when COO Ron Beaumont presented several slides on it to them. One board member approached Sullivan privately to question the program. When Sullivan broached the subject with Ebbers, Ebbers told Beaumont and Sullivan that the next board presentation should be at a higher level and not include "Close the Gap" information. Beaumont's next board

presentation, in September 2001, did not include any information about the "Close the Gap" program.

h) *Fourth Quarter 2001*

By the fourth quarter of 2001, even the "Close the Gap" program could not generate enough one-time revenue opportunities to create double-digit revenue growth. Nor could the staff find ways to adjust the line cost expenses sufficient to hit the earnings target. After Myers capitalized over $941 million in line costs, the accounting staff still had to adjust the SG&A (sales, general, and administrative) expenses in order to reach the target. On the fourth quarter earnings conference call, Ebbers assured investors that "[w]e stand by our accounting," and later said in a CNBC interview that "[w]e've been very conservative on our accounting."

i) *First Quarter 2002*

WorldCom's revenue declined in the first quarter of 2002. The accounting staff added new sources of revenue to improve the results but were unable to bring the revenue up to analysts' expectations. Sullivan informed Ebbers that even with the improper revenue adjustments and the capitalization of line costs, the company would be unable to meet investors' expectations that quarter. The accounting staff capitalized about $818 million in line costs, but WorldCom still had to announce that its results had fallen below investors' expectations.

Appendix A

j) *Investigation, Trial, and Sentence*

In March 2002, the Securities and Exchange Commission ("SEC") began to investigate WorldCom. At the end of April 2002, WorldCom's board asked Ebbers to resign, which he did on April 29th. Ebbers began to liquidate some of his assets in order to pay back his debts, but during May 2002 he also bought three million more shares of WorldCom stock. A month after Ebbers' departure, WorldCom's Internal Audit Department learned of the line cost capitalization, and alerted the new CEO. Sullivan was soon fired, and WorldCom disclosed the fraud to the public on June 25, 2002. WorldCom's stock collapsed, losing 90% of its value, and the company filed for bankruptcy.

On September 15, 2004, Ebbers was charged in a superseding indictment with one count of conspiracy to commit securities fraud and related crimes, one count of securities fraud, and seven counts of making false filings with the SEC. *See* 18 U.S.C. § 371 (conspiracy); 15 U.S.C. §§ 78j (b) & 78ff (securities fraud); 15 U.S.C. §§ 78m(a) & 78ff (false filings).

A jury convicted Ebbers on all counts on March 15, 2005. The pre-sentence report ("PSR") recommended a base offense level of six, plus sentencing enhancements of 26 levels for a loss over $100 million, of four levels for involving more than 50 victims, of two levels for receiving more than $1 million from financial institutions as a result of the offense, of four levels for leading a criminal activity involving five or more participants, and of two levels for abusing a position of public trust, bringing the total offense level to 44 levels.

The government also sought a two-level enhancement for obstruction of justice on the basis of Ebbers' having testified contrary to the jury's verdict. With Ebbers' criminal history category of I, the Guidelines range calculated in the PSR was life imprisonment. The Probation Department recommended a 30-year sentence. Judge Jones declined to apply the enhancements for deriving more than $1 million from financial institutions or for obstruction of justice. She also denied Ebbers' motions for downward departures based on the claims that, *inter alia*, the loss overstated the seriousness of the offense, his medical condition was poor, and he had performed many beneficial community services and good works. She determined that his total offense level was 42 and that the advisory Guidelines range would be 30 years to life. She then sentenced Ebbers to 25 years' imprisonment and three years' supervised release, and imposed a $900 special assessment but no fines.

This appeal followed.

DISCUSSION

Ebbers argues that: (i) he was deprived of a fair trial when the government refused to immunize certain potential witnesses and the district court erred in its rulings on related issues; (ii) the court should not have charged the jury on conscious avoidance; (iii) the government should have been required to allege and prove violations of GAAP; and (iv) the sentence imposed is unreasonable.

Appendix A

a) *Selective Immunization of Witnesses*

Ebbers contends that he was denied a fair trial because the government granted immunity only to witnesses whose testimony incriminated him and not to witnesses whose testimony would exculpate him but who would have invoked the privilege against self-incrimination if called to testify. This alleged selective immunization was aggravated in his view by the government's eliciting hearsay testimony from immunized witnesses as to statements of the non-immunized witnesses on a co-conspirator theory. Fed.R.Evid. 801(d)(2)(E). He finally asserts that the district court erred in substantially denying his motion to impeach the alleged co-conspirator statements with prior admissions and in declining to give a "missing witness" instruction to the jury with regard to the non-immunized witnesses.

1. Standard of Review

We have not previously adopted a standard of review for district court decisions not to compel the government to choose between giving use immunity to defense witnesses or forgoing its own use of immunized testimony. At least three other circuits have applied the abuse of discretion standard to such determinations. *United States v. Burke*, 425 F.3d 400, 411 (7th Cir.2005); *United States v. Perez*, 280 F.3d 318, 348 (3d Cir.2002); *United States v. LaHue*, 261 F.3d 993, 1015 (10th Cir.2001). *But see United States v. Alvarez*, 358 F.3d 1194, 1216 (9th Cir.2004) (applying *de novo* review to issue except to findings of fact, which are reviewed for clear error). Following those circuits, we also adopt an abuse of discretion standard.

Such a decision requires consideration whether "(1) the government has engaged in discriminatory use of immunity to gain a tactical advantage or, through its own overreaching, has forced the witness to invoke the Fifth Amendment; and (2) the witness' testimony will be material, exculpatory and not cumulative and is not obtainable from any other source." *United States v. Burns*, 684 F.2d 1066, 1077 (2d Cir.1982) (citations omitted). Therefore, a district court must find facts as to the government's acts and motives and then balance factors relating to the defendant's need for the evidence and its centrality, or lack thereof, to the litigation. Factual findings would of course be reviewed under the clear error rule. *United States v. Lucien*, 347 F.3d 45, 53 (2d Cir.2003). *De novo* review of the balancing analysis would not be appropriate because trial courts have a comparative advantage over appellate courts when it comes to weighing the needs of the parties and the centrality of particular pieces of evidence to a trial. *Cf. Percy v. San Francisco General Hospital*, 841 F.2d 975, 978 (9th Cir.1988). Therefore, we adopt the abuse of discretion standard to the balancing analysis.

2. The Immunity Issue

The government is under no general obligation to grant use immunity to witnesses the defense designates as potentially helpful to its cause but who will invoke the Fifth Amendment if not immunized. *United States v. Turkish*, 623 F.2d 769, 774 (2d Cir.1980) (discussing difference between prosecutorial powers and obligations and those of a defendant). *See also United States v. Praetorius*, 622 F.2d 1054, 1064 (2d Cir.1979) (refusing to require the government to confer use immunity absent "extraordinary circumstances").

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A grant of use immunity may well hamper the government in a future prosecution of a witness. *United States v. Todaro*, 774 F.2d 5, 9 (2d Cir.1984). In such a prosecution, the government would have to show that the immunized testimony was not the source of any evidence it presents, *Kastigar v. United States*, 406 U.S. 441, 460, 92 S.Ct. 1653, 32 L.Ed.2d 212 (1972), and that the testimony of government witnesses was not tainted by their knowledge of the immunized testimony, *see United States v. North*, 920 F.2d 940 (D.C.Cir.1990). Although the government may gain protection in completed investigations by establishing a record of the evidence collected before the immunized testimony is given, it may have difficulty shielding all its potential witnesses from that testimony.

However, the ability to give immunity to one witness but not another is a potentially powerful tool for a prosecutor, particularly in light of the prosecutor's ability to create incentives for witnesses to invoke the privilege against self-incrimination. *United States v. Dolah*, 245 F.3d 98, 106 (2d Cir.2001), *abrogated on other grounds by Crawford v. Washington*, 541 U.S. 36, 124 S.Ct. 1354, 158 L.Ed.2d 177 (2004). There are, therefore, limits on the government's use of immunity.

In an extreme case, a court might hold that the absence of the non-immunized witness caused the government's evidence to fall short of proof beyond a reasonable doubt. In addition, a court may order the prosecution to choose between forgoing the testimony of an immunized government witness or granting use immunity to potential defense witnesses. *See United States v. Horwitz*, 622 F.2d 1101, 1105-06 (2d

Cir.1980); *Dolah*, 245 F.3d at 105. To obtain such an order, a defendant must make a two-pronged showing. *United States v. Diaz*, 176 F.3d 52, 115 (2d Cir.1999).

First, the defendant must show that the government has used immunity in a discriminatory way, *id.* at 115, has forced a potential witness to invoke the Fifth Amendment through "overreaching," *id.*, or has deliberately denied "immunity for the purpose of withholding exculpatory evidence and gaining a tactical advantage through such manipulation." *Id.*

We have said that a discriminatory grant of immunity arguably may be no more than "a decision . . . to confer immunity on some witnesses and not on others." *Dolah*, 245 F.3d at 105-06. However, it may also be the case that the immunity decisions in question are so obviously based on legitimate law enforcement concerns — e.g., granting immunity to a witness who has pleaded guilty and has been sentenced to substantial jail time while denying it to a principal target of the ongoing criminal investigation — that it is clear that a court cannot intervene without substantially hampering the administration of justice.

Prosecutorial "overreaching" can be shown through the use of "threats, harassment, or other forms of intimidation [which have] effectively forced the witness to invoke the Fifth Amendment." *Blissett v. Lefevre*, 924 F.2d 434, 442 (2d Cir.1991). The "manipulation" standard overlaps to a degree with the discrimination test but involves an express finding of a tactical purpose on the government's part. *Id.*

Second, the defendant must show that the evidence to be given by an immunized witness "will be material, exculpatory and not cumulative and is not obtainable from any other source." *Burns*, 684 F.2d at 1077. In that regard, exculpatory evidence is material when it "tends to show that the accused is not guilty." *United States v. Gil*, 297 F.3d 93, 101 (2d Cir.2002) (citing *In re United States (Coppa)*, 267 F.3d 132, 139 (2d Cir.2001)). The bottom line at all times is whether the non-immunized witness's testimony would materially alter the total mix of evidence before the jury.

In particular, Ebbers argues that the testimony of WorldCom COO Ronald Beaumont, Vice President for Financial Reporting Stephanie Scott, and Vice President Ronald Lomenzo would have exculpated him by showing that there were no " 'red flags' that would have made WorldCom personnel outside the Accounting Department aware of any fraud," by denying that they had made the statements attributed to them by the government's witnesses, and by providing testimony "about actions by Ebbers inconsistent with awareness of impropriety."

Whether Ebbers meets the first prong of the test is in doubt. Arguably, the immunity decisions were consistent with legitimate law enforcement concerns. Of the six immunized government witnesses, three pled guilty and received jail sentences, and a fourth pled guilty but was not incarcerated. The remaining two were useful but not critical to the government's case and were not central players in the criminal scheme. As the ensuing discussion makes clear, Beaumont, Scott, and Lomenzo, whose "I knew nothing" defenses were in tension with the executive positions they

held at WorldCom, were necessarily legitimate targets of the investigation. There is no evidence of "overreaching" or the manipulation of immunity expressly for tactical reasons. Ebbers' claim in this regard therefore relies heavily on *Dolah*'s remark that "discriminatory use" of immunity is arguably no more than "simply a decision . . . to confer immunity on some witnesses and not on others." *Dolah*, 245 F.3d at 105-06.

We do not resolve that issue, however, because Ebbers has not shown that the absence of testimony by Beaumont, Scott, or Lomenzo affected the total mix of evidence before the jury. There was therefore no abuse of discretion in denying Ebbers' requests. We discuss the potential testimony of each of those witnesses in turn.

(i) Beaumont

Ebbers suggests[1] that, if immunized, WorldCom Group COO Ronald Beaumont would have testified that: (i) WorldCom's 3Q 2000 reported results were accurate; (ii) Beaumont had no knowledge of the reserve release in 2000; (iii) therefore Sullivan falsely stated that Beaumont had told Sullivan and Ebbers in March 2001 "we don't have reserves to take like we did last year"; (iv) in another conversation, a reference by Beaumont to "Scott's stuff" did not refer to line cost capitalization; and (v) again contrary to

1. Ebbers has the FBI reports of interviews with various potential witnesses and has drawn upon them to give factual support to his selective immunization claim. These reports have also been provided to us under seal, and, where necessary, we paraphrase their contents.

Sullivan's testimony, Ebbers instructed Beaumont to include the breakdown of "Close the Gap" items in the second quarter 2001 Board presentation.

However, there is no basis to conclude that Beaumont would have been a witness helpful to appellant. As for (i), Beaumont's purported opinion that the 3Q 2000 report was accurate, the issue concerned the reserve release, but nothing in the record before us, *see* Note 1 *supra*, indicates what Beaumont's opinion was regarding whether the release of the reserves was proper or improper.

Moreover, even if Beaumont believed that the reserve release was proper and would have so testified, that testimony would not have been helpful to appellant. As argued by the government, the underlying issue was whether Ebbers knew of the prior reserve release and the lack of other reserves and, because of that lack, authorized the capitalization of line costs. Beaumont's opinion as to the propriety of the release therefore did not undercut the government's case.

It is true that, if Beaumont claimed ignorance of the reserve release, he could not have said to Ebbers in March 2001, "We don't have reserves to take like we did last year." However, the jury was highly unlikely to credit any such claim of ignorance of the reserve release and denial of Sullivan's testimony that Beaumont told Ebbers of the lack of further reserves. An April 2001 email message from Beaumont to Myers was in evidence that stated "last year we released a good deal of reserves which we don't have this year to release." This message surely would have devastatingly refuted any testimony by Beaumont that he could not have said anything about the reserves to Ebbers.

Sullivan had also testified that, in a conversation with Beaumont at which Ebbers was present, Beaumont had discussed the line cost capitalization, stating that part of the capital budget was reserved for "Scott's stuff." Ebbers contends that, had Beaumont testified, he would have denied that the reference to "Scott's stuff" referred to line cost capitalization.

Ebbers claims that this testimony would have been helpful to him in two ways. First, it would show that the specific conversation did not involve line costs. Second, Beaumont's ignorance of the frauds is evidence that Sullivan kept others, including Ebbers himself, in the dark. We are unpersuaded.

First, the record basis for expecting Beaumont to give such testimony is that, in his interview with the FBI, Beaumont claimed ignorance of the capitalizing of line costs until May 2002. Ebbers infers from this that Beaumont would have denied that "Scott's stuff" referred to line cost capitalization although Beaumont never discussed the use of that phrase in his interview. In any event, such testimony would have been highly self-serving and of dubious credibility. One of Beaumont's major responsibilities as COO was to prepare the capital expenditure budget and find ways to reduce it. To credit such testimony, the jury would have had to believe that he had no idea what was in that budget.

Second, Beaumont's testimony, even if credited, would not have shown what Sullivan and Ebbers understood "Scott's stuff" to be.

Third, Ebbers' argument that Sullivan kept all top management in the dark, including Ebbers, as to the various financial reporting frauds, and that Beaumont's assertions of ignorance show this, simply doesn't wash. Beaumont did not become COO until January 2001, and his ignorance of prior frauds would not show that the CEO was similarly ignorant. In any event, even if Sullivan kept Beaumont in the dark, that fact would not show Ebbers' ignorance. Keeping the COO in the dark is different from keeping the CEO in the dark. Moreover, if Sullivan acting alone would have had a motive to conceal the scheme from Beaumont, Sullivan and Ebbers acting in concert may well have had a similar motive.

Appellant also suggests that Beaumont would have testified that Ebbers told him to include a slide in the 2Q 2001 Board presentation about the "Close the Gap" program and that Beaumont would have defended the "Close the Gap" process as proper. Ebbers argues that if "the jury [had] known that WorldCom's COO denied knowledge of the fraud and directly refuted Sullivan's claims that he, Ebbers and Sullivan had conspiratorial conversations, the outcome of this trial would likely have been different."

We disagree. The jury knew that a "Close the Gap" slide was included in the 2Q 2001 presentation, and Beaumont's testimony that Ebbers told him to put it in would hardly have been exculpatory. The jury also knew that Ebbers claimed to believe the "Close the Gap" program was proper, and Beaumont's self-serving agreement would have added nothing. Moreover, Beaumont gave no explanation in his interview for why the "Close the Gap" information was not

included in subsequent board presentations. In sum, we cannot conclude that Beaumont would have been a witness helpful to Ebbers.

(ii) Scott

Stephanie Scott was WorldCom's Vice President for Financial Reporting from 2000 through late 2002. Ebbers argues that, if immunized, she would have countered Lisa Taranto's testimony that Scott ordered changes to the monthly revenue reports presented to Arthur Andersen, WorldCom's outside accounting firm. Also, Scott could have denied participating in the line cost fraud. Taranto testified that around Q3 of 2001, Scott asked her to "create a new version of the Mon Rev [a monthly report] and to remove some items that were in the corporate unallocated line item, and to reclass them into the appropriate sales channels that they related to." Our review of Scott's interview with the government indicates that her testimony would have differed only as to which quarter she might have asked Taranto to correct the corporate unallocated items. That is not an inconsistency of significance.

As for Scott's potential testimony that she was unaware of the line cost adjustments, Sullivan testified that he had spoken to Scott about capitalizing the line costs and that she told him it would not be legitimate accounting. Because there was no testimony that Ebbers was present for any such conversation between Sullivan and Scott or was aware of it, this contradiction of Sullivan is hardly exculpatory of Ebbers. And, while Scott's testimony would have contradicted Sullivan's, Scott's version was entirely self-serving and of little, if any, value as an impeachment of Sullivan.

Ebbers also argues that, if Scott was unaware of the line cost capitalization, Ebbers' claim that he was also unaware of it would be strengthened. For the same reasons discussed with regard to Beaumont's testimony, Scott's testimony in this regard would not have been helpful.

(iii) Lomenzo

Appellant claims that Ronald Lomenzo, a WorldCom Vice President who reported directly to Sullivan, "would have testified that (1) the 'Close the Gap' program was employed to 'ensure that all revenue was captured,' [and] (2) neither the pressure to record revenue nor the number of revenue adjustments increased in 2001." Lomenzo described the "Close the Gap" program to the government as one used by others in WorldCom's management to monitor his efforts at capturing all revenue opportunities. He said that he was not personally involved in it. Sullivan had testified about the "Close the Gap" program, described it as a "more formalized" and larger version of Lomenzo's revenue opportunities list, but never designated Lomenzo as involved in the program. Because Lomenzo was not directly involved in the program, his (self-serving) testimony about his understanding of its purpose would have had little, if any, probative value regarding its actual purpose.

As for whether the pressure to record revenue and revenue adjustment increased during 2001, Lomenzo's claim that he felt no greater pressure to meet revenue targets in 2001 than in 2000 is not probative of Ebbers' or Sullivan's state of mind. Furthermore, Lomenzo's account of Sullivan and Myers attempting to convince him to release $370 million

in line cost reserves in 2000 indicates that the pressure over revenues was already high in 2000.

We therefore conclude that Lomenzo's testimony would not have been materially helpful to Ebbers.

b) *Impeaching Co-Conspirator Statements under FRE 806*

We review a district court's evidentiary rulings for abuse of discretion, and will reverse only if we find that there was a violation of a substantial right. *Marcic v. Reinauer Transp. Cos.*, 397 F.3d 120, 124 (2d Cir.2005).

Rule 806 states in relevant part that "[w]hen a hearsay statement ... has been admitted in evidence, the credibility of the declarant may be attacked, and if attacked may be supported, by any evidence which would be admissible for those purposes if declarant had testified as a witness." Fed.R.Evid. 806. Ebbers argues that he should have been allowed to impeach Beaumont's hearsay statement that " 'we don't have reserves to take like we did last year . . . so we've got some real cutting to do in [the line cost] area,' " with evidence that Beaumont was not involved in that reserve release. The district court concluded that there was no contradiction because Beaumont might have learned of the releases later. We agree.

Beaumont did state that he would have had to approve a reserve release that large and did not, but it is unclear from the interview notes whether Beaumont was referring to a release in 2000, before he was COO, or 2001, after he was COO. Because Beaumont presumably had no role in

approving reserve releases in 2000 while President of WorldCom's Network Services division, and Sullivan was testifying about Beaumont's statement about the 2000 releases, Sullivan's testimony would not have been impeached by the quoted language from Beaumont's interview. *See United States v. Trzaska*, 111 F.3d 1019, 1024-25 (2d Cir.1997) (citing two tests to determine inconsistency: "any variance between the statement and testimony that has a reasonable bearing on credibility" (citations and emphasis omitted), and "could the jury reasonably find that a witness who believed the truth of the facts testified to would have been unlikely to make a statement of this tenor" (citation omitted)).

Ebbers also contends that he should have been allowed to impeach "testimony that Beaumont complied with a direct order from Ebbers to remove a 'Close the Gap' slide from a Board of Directors presentation" with "Beaumont's prior statements that no one had instructed him to remove the slide from the presentation at issue and, in fact, Ebbers had instructed him to include a 'Close the Gap' slide in a prior Board Presentation." Sullivan testified that "[t]here was a conversation between Bernie, Ron Beaumont and myself, where Bernie told us to keep the presentations at a higher level, that our jobs were on the line, and he told Ron Beaumont not to get into close the gap items for the third quarter of 2001." Sullivan then testified that Beaumont did not present a "Close the Gap" slide at the 3Q 2001 board meeting. However, he did not testify to any statements by Beaumont on the matter, and therefore no hearsay statement by Beaumont was introduced that might have been impeached under Rule 806.

Ebbers next argues that he should have been allowed to impeach "Beaumont's alleged co-conspirator statement that a large portion of WorldCom's capital expenditures budget was dedicated to 'Scott's stuff,' an alleged reference to the line cost capitalization" with "evidence that Beaumont had previously told the government that his statement 'was never tied to capitalized line costs'. . . ." In denying the attempted impeachment, the district court ruled that Ebbers was attempting to impeach Sullivan's understanding of Beaumont's statement, rather than the content of the statement itself. Because Sullivan testified that Beaumont did not clarify what was meant by "Scott's stuff" at the meeting, Beaumont's purported statement would not have been expressly contradicted by his profession of ignorance of line cost capitalization. Sullivan was subject to cross-examination as to his own understanding of "Scott's stuff," and we therefore find no violation of substantial rights.

Finally, Ebbers claims that he should have been allowed to impeach "Scott's alleged co-conspirator statement that she instructed Taranto to create a special MonRev in order 'to minimize the amount of revenue items that were corporate unallocated for her presentation to Arthur Anderson' " with her statements to the government. As discussed above, her statement to the government was not materially inconsistent with Taranto's testimony, and there was no violation of substantial rights.

c) *Missing Witness Instruction*

Ebbers requested that a missing witness instruction be given to the jury regarding Beaumont, Lomenzo and Scott,

but the district court denied it. We review a district court's refusal to provide a requested missing witness instruction for abuse of discretion and actual prejudice. *United States v. Gaskin*, 364 F.3d 438, 463 (2d Cir.2004).

In *Myerson*, we stated that "in the absence of circumstances that indicate the government has failed to immunize an exculpatory witness, a district court does not abuse its discretion by refusing to give a missing witness charge." *United States v. Myerson*, 18 F.3d 153, 160 (2d Cir.1994). For reasons discussed, none of the three proposed witnesses would have exculpated Ebbers, and the district court did not err in refusing to give a missing witness charge.

d) *Conscious Avoidance Charge*

"A conscious-avoidance charge is appropriate when (a) the element of knowledge is in dispute, and (b) the evidence would permit a rational juror to conclude beyond a reasonable doubt that the defendant was aware of a high probability of the fact in dispute and consciously avoided confirming that fact." *United States v. Hopkins*, 53 F.3d 533, 542 (2d Cir.1995) (citations and internal quotation marks omitted). "We review a claim of error in jury instructions *de novo*, reversing only where, viewing the charge as a whole, there was a prejudicial error." *United States v. Aina-Marshall*, 336 F.3d 167, 170 (2d Cir.2003).

At trial, Ebbers testified as follows

> Q: Did you ever believe that any of the statements contained in those public filings were not true?
>
> A: No, sir.

Appendix A

Q: Did you ever believe that WorldCom had reported revenue that it was not entitled to report?

A: No, sir.

Q: Did you ever believe that WorldCom had an obligation to announce changes in accounting practices that it had failed to announce?

A: No, sir.

Q: Did you ever believe that WorldCom was putting out bad numbers in its financial statements in any way at all?

A: No.

He also denied that he knew about discrepancies in the actual and reported line costs; that Sullivan had told him he would make a transfer of line costs to lower the reported number; that he looked at the SG&A reports he was sent; that he knew of improper entries made in the books; that he knew of the special MonRev report given to the accountants; and that he thought any of the "Close the Gap" process was illegitimate. The first prong of the test, that knowledge be disputed, is therefore easily met.

The evidence that Ebbers either actually knew or was aware of the high probability that the financial statements were false was not limited to Sullivan's testimony, as Ebbers claims. Ebbers testified that he attended some of the line cost meetings, that he read the preliminary and final MonRev reports, and that he went to "Close the Gap" meetings with Sullivan and Beaumont. He also testified to practices that

would allow a jury to find that he was consciously avoiding information: using a procedure for signing documents he didn't bother to read in full, including the 10-Ks, and tossing the management budget variance report in the trash without reading it.

The district court found that Ebbers' own testimony rendered the instruction proper, because, based on that testimony, a rational juror could find he was consciously trying to avoid knowledge that the financial reports were inaccurate. We agree.

e) *The Need to Prove GAAP Violations*

Ebbers argues that the indictment was flawed because it did not allege that the underlying accounting was improper under GAAP,[2] and that the district court should have required the government to prove violations of GAAP at trial. He claims that where a fraud charge is based on improper accounting, the impropriety must involve a violation of GAAP, because financial that comply with GAAP necessarily meet SEC disclosure requirements. *See Ganino v. Citizens Utilities Co.*, 228 F.3d 154, 160 n. 4 (2d Cir.2000) ("The SEC treats the FASB's standards as authoritative."); 17 C.F.R. § 210.4-01(a)(1) ("Financial statements filed with the [SEC]

2. Generally Accepted Accounting Principles ("GAAP") are the official standards adopted by the American Institute of Certified Public Accountants (the "AICPA"), a private professional organization, through three successor groups it established: the Committee on Accounting Procedure, the Accounting Principles Board (the "APB"), and the Financial Accounting Standard Board (the "FASB"). *Ganino v. Citizens Utilities Co.*, 228 F.3d 154, 160 n. 4 (2d Cir.2000).

which are not prepared in accordance with generally accepted accounting principles will be presumed to be misleading or inaccurate. . . ."). Before trial he moved to dismiss the indictment on those grounds, and after trial moved for judgment of acquittal pursuant to Federal Rule of Criminal Procedure 29 based on the Government's failure to prove violations of GAAP at trial. The district court denied both motions. We review both the denial of a motion to dismiss an indictment and the denial of a Rule 29 motion for judgment of acquittal de novo. *United States v. Florez*, 447 F.3d 145, 154 (2d Cir.2006); *United States v. Yousef*, 327 F.3d 56, 137 (2d Cir.2003).

We addressed a similar argument in *United States v. Simon*, 425 F.2d 796, 805-06 (2d Cir.1969) (Friendly, J.), when three accountants asked for a jury instruction that they could not be found guilty of securities fraud if the financial statements in question were in compliance with GAAP. We ruled that the district court properly refused to give the instruction.

We see no reason to depart from *Simon*. To be sure, GAAP may have relevance in that a defendant's good faith attempt to comply with GAAP or reliance upon an accountant's advice regarding GAAP may negate the government's claim of an intent to deceive. *Id.* at 805. Good faith compliance with GAAP will permit professionals who study the firm and understand GAAP to accurately assess the financial condition of the company. This can be the case even when the question of whether a particular accounting practice complies with GAAP may be subject to reasonable differences of opinion.

However, even where improper accounting is alleged, the statute requires proof only of intentionally misleading statements that are material, *i.e.*, designed to affect the price of a security. 15 U.S.C. § 78ff. If the government proves that a defendant was responsible for financial reports that intentionally and materially misled investors, the statute is satisfied. The government is not required in addition to prevail in a battle of expert witnesses over the application of individual GAAP rules.

For example, an addition to revenue used in the "Close the Gap" program may or may not have been improper under particularized GAAP rules. However, where an addition intentionally involved funds that had not previously been used to calculate revenue and were a one-time addition to revenue, investors would not have been alerted to the fact that revenue as previously calculated was actually down. Such an intentionally misleading financial statement violates the statute. For similar reasons, the addition of underusage penalties to revenue may or may not have been proper under some GAAP rule, but was intentionally misleading because the penalties were not expected to be realized. Finally, appellant claims that capitalization of some leases may have been proper under GAAP, but the capitalization of line costs — again an unannounced change in bookkeeping — was based not on an examination of particular leases but on the financial targets needed to keep share price high.

In a real sense, by alleging and proving that the financial statements were misleading, the government did, in fact, allege and prove violations of GAAP. According to the AICPA's Codification of Statements on Accounting

Standards, AU § 312.04, "[f]inancial statements are materially misstated when they contain misstatements whose effect, individually or in the aggregate, is important enough to cause them not to be presented fairly, in all material respects, in compliance with GAAP." Thus, GAAP itself recognizes that technical compliance with particular GAAP rules may lead to misleading financial statements, and imposes an overall requirement that the statements as a whole accurately reflect the financial status of the company.

To be sure — and to repeat — differences of opinion as to GAAP's requirements may be relevant to a defendant's intent where financial statements are prepared in a good faith attempt to comply with GAAP. The rules are no shield, however, in a case such as the present one, where the evidence showed that accounting methods known to be misleading — although perhaps at times fortuitously in compliance with particular GAAP rules — were used for the express purpose of intentionally misstating WorldCom's financial condition and artificially inflating its stock price.

f) *Reasonableness of Sentence*

With regard to his sentence, Ebbers urges that the district court's loss calculation was incorrect and that his sentence was unreasonably long. After Booker, we review a district court's conclusions of law de novo, its application of the Guidelines on issues of fact for clear error, and its exercise of discretion with respect to departures for abuse of that discretion. *United States v. Fuller*, 426 F.3d 556, 562 (2d Cir. 2005).

Appendix A

1. Loss Calculation

The district court applied the loss calculation from then-applicable the fraud Guidelines at U.S.S.G. § 2B1.1 (2001). No detailed definition of loss relevant to the issues before us is set out in the Guidelines. The Commentary does state, "The court need only make a reasonable estimate of the loss." U.S. Sentencing Guidelines Manual § 2B1.1 cmt. 2(c) (2001). Moreover, where fraud in investments is concerned, the loss to a buyer or seller who relied upon the fraud is not to be reduced by the gain to an innocent seller or buyer on the other side of the transaction. *Id.* at cmt. 2(F)(iv). In this case, therefore, the loss is that suffered by those investors who bought or held WorldCom stock during the fraud period either in express reliance on the accuracy of the financial statements or in reliance on what *Basic, Inc. v. Levinson* described as the "integrity" of the existing market price. 485 U.S. 224, 247, 108 S.Ct. 978, 99 L.Ed.2d 194 (1988).

Determining this amount is no easy task. One version of the so-called market capitalization test would, in its simplest form, take the share price on the date of a fraudulent statement — X-day, we shall call it — subtract from it the share price on the day after the fraud is revealed — Y-day — and multiply that amount by the number of outstanding shares.

There is a problem, however, with this simplistic analysis. If the truth had been told on X-day, shareholder A would have suffered an immediate loss commensurate with the fraud loss because potential buyers at the earlier price would have immediately disappeared upon the bad news. When perpetrated, therefore, the fraud would not damage A

any more than the truth, at least immediately. However, were investor B to buy the stock after the fraudulent statement and in reliance upon the integrity of the market price, B would suffer a loss in the amount of the price paid less the intrinsic value, which, under the market capitalization test, would usually be deemed to be the price after the disclosure of the fraud on Y-day.

While shareholder A is as damaged by the truth as by the fraud on X-day, many frauds are ongoing, and, contrary to the testimony of Ebbers' expert, shareholder A may suffer a loss over time in being misled in assessing whether to hold or sell the stock. While A can be said not to have lost anything as a result of the fraud on X-day — assuming no prior disclosure obligation on the defendant's part — if new fraudulent statements are issued on X+1, X+2, etc., and the company's true value has further diminished on each occasion, the succeeding X-day frauds would have the effect of preventing A from making an informed judgment about holding the stock.

The securities laws are intended to allow investors to buy, sell, or hold based on accurate information. An investor who buys securities before an extended fraud begins, and holds them during the period of the fraud, may therefore be little different from one why buys in mid-fraud.

For example, the ongoing fraud here involved a series of periodic, fraudulent financial reports that systematically inflated WorldCom's operating profits. If the first report had been accurate, some decrease in fundamental value would have been revealed, but the decrease would have been far

less than that revealed in June 2002 after several more fraudulent reports. Investors who held their stock throughout the fraud period were therefore denied the opportunity to reassess and perhaps sell according to their own informed estimates of the declining performance.

The loss to investors who hold during the period of an ongoing fraud is not easily quantifiable because we cannot accurately assess what their conduct would have been had they known the truth. However, some estimate must be made for Guidelines' purposes, or perpetrators of fraud would get a windfall. Moreover, revelation of an extended period of fraudulent financial statements may cause losses beyond that resulting from the restatement of financial circumstances because confidence in management and in even the truthful portions of a financial statement will be lost. *AUSA Life Ins. Co. v. Ernst & Young*, 206 F.3d 202, 230 (2d Cir.2000) (Winter, C.J., dissenting) ("Reasonable investors surely view firms with an untrustworthy management and auditor far more negatively than they view financially identical firms with honest management and a watch-dog auditor."). Credit may become totally unavailable even where an otherwise viable firm remains.

Worse, there is another variable. The loss must be the result of the fraud. *United States v. Olis*, 429 F.3d 540, 547 (5th Cir. 2005). Many factors causing a decline in a company's performance may become publicly known around the time of the fraud and be one cause in the difference in price between X-day and Y-day. *Id.* at 548 (explaining that numerous factors, not just defendant's fraud, contributed to stock price decline). For example, the dot-com bubble burst

and its likely negative future effect on WorldCom's business was public knowledge. The effect of that knowledge would be a downward pressure on share price not attributable to the defendant. Losses from causes other than the fraud must be excluded from the loss calculation. *Id.* at 547.

Other complications would undoubtedly appear in a case where more than the grossest calculation is needed. This is not such a case. All of Ebbers' arguments with regard to the loss calculation encounter a hard fact. A 26-level loss calculation has a $100 million threshold, which is easily surpassed under any calculation. For example, the Probation Office calculated the loss at $2.23 billion, based on a price of $0.83/share on June 25, 2002, when the company announced the improper accounting and restated its results, and the price on July 1, 2002, $0.06. There were about 2.9 billion shares of WorldCom stock outstanding on June 25, 2002. *Id.* Even excluding the 20,436,193 shares owned by Ebbers, the 5,000 shares owned by Sullivan, and shares owned by other guilty executives, there was still a $2.2 billion loss to investors not involved in the conspiracy, using the Probation Office's estimate of 77 cents loss per share.

To be sure, this calculation is flawed. Ebbers' expert testified that at least some of the decline in WorldCom's stock price immediately after June 25, 2002, was attributable to factors other than accounting fraud, citing "(1) planned sharp reductions in capital expenditures, (2) lay-offs affecting 17,000 employees, (3) the abandonment of non-core businesses, and (4) the deferral or elimination of dividends." His expert estimated that these other factors might have been responsible for 35% or more of the stock decline.

Even so, the loss amount is still well above $1 billion, or ten times greater than the $100 million dollar threshold for the 26-level enhancement. U.S. Sentencing Guidelines Manual § 2B1.1 (2001). Moreover, it is probably the case that large numbers of investors holding shares on June 25, 2002, had either held the shares during the period when the repeated fraudulent financial statements were used or had bought them during the scheme at prices much higher than 83¢ per share. And neither their loss nor those of bondholders — estimated by the Probation Office at $10 billion — is included in the Probation Office's calculations. Even a loss calculation of $1 billion is therefore almost certainly too low, and there is no reasonable calculation of loss to investors that would call for a remand.[3]

2. Sentence Disparities

Ebbers argues that his sentence should have been closer to those imposed on his co-defendants: CFO Scott Sullivan, who received five years; Controller David Myers, who received one year and one day; Accounting Director Buford Yates, who received one year and one day; Director of Management Reporting Betty Vinson, who received five

3. Ebbers relies upon *United States v. Canova*, 412 F.3d 331, 355-56 (2d Cir.2005), for the proposition that a $5 million error in the calculation of the loss amount is sufficient to support a remand for resentencing. However, in that case the total loss alleged by the government was $5 million, which would have enhanced the defendant's offense level by thirteen levels, and the district court erred in declining to add any loss enhancement. *Id.* at 355. While a $5 million calculation error is obviously significant in such a case, no putative error here is of remotely comparable significance. *See* U.S. Sentencing Guidelines Manual § 2B1.1 (2001).

months; and Director of Legal Entity Accounting Troy Normand, who received three years on probation.

District courts must consider "the need to avoid unwarranted sentence disparities among defendants with similar records who have been found guilty of similar conduct," 18 U.S.C. § 3553(a)(6), and we may remand cases where a defendant credibly argues that the disparity in sentences has no stated or apparent explanation. *See United States v. McGee*, 408 F.3d 966, 988 (7th Cir.2005) (remanding for reconsideration of sentencing disparities between equally culpable codefendants). However, a reasonable explanation of the different sentences here is readily apparent, namely, the varying degrees of culpability and cooperation between the various defendants. All of those named above cooperated and pled guilty. Ebbers did not. Moreover, each was a subordinate of Ebbers. Ebbers, as CEO, had primary responsibility for the fraud.

3. Reasonableness

At oral argument, the overall reasonableness of the sentence was raised by the court. Twenty-five years is a long sentence for a white collar crime, longer than the sentences routinely imposed by many states for violent crimes, including murder, or other serious crimes such as serial child molestation. However, Congress has directed that the Guidelines be a key component of sentence determination. Under the Guidelines, it may well be that all but the most trivial frauds in publicly traded companies may trigger sentences amounting to life imprisonment — Ebbers' 25-year sentence is actually below the Guidelines level. Even

the threat of indictment on wafer-thin evidence of fraud may therefore compel a plea. For example, a 15¢ decline in share price in a firm with only half the number of outstanding shares that WorldCom had would constitute a loss of $200 million. No matter how many reasons other than the fraud may arguably account for the decline, a potential defendant would face an enormous jeopardy, given the present loss table, and enhancements for more than 250 victims, for being a leader of a criminal activity involving 5 or more participants, and for being an officer of the company.[4]

However, the Guidelines reflect Congress' judgment as to the appropriate national policy for such crimes, *United States v. Rattoballi*, 452 F.3d 127, 2006 WL 1699460, at *5 (2d Cir. June 21, 2006) (stating that the court will "continue to seek guidance from the Sentencing Commission as expressed in the Sentencing Guidelines and authorized by Congress.") (citation omitted), and Ebbers does not argue otherwise.

Moreover, the securities fraud here was not puffery or cheerleading or even a misguided effort to protect the company, its employees, and its shareholders from the capital-impairing effects of what was believed to be a temporary downturn in business. The methods used were specifically

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4. U.S. Sentencing Guidelines Manual § 2B1.1 (2005) (setting the offense level of 28 for a loss of $200 million or more, 6 levels for a crime involving 250 or more victims, and 4 levels for being the officer of a publicly traded company); § 3B1.1 (2005) (adding 4 levels for leading a criminal activity with five or more participants); Sentencing Table (2005) (setting the sentence at thirty years to life for an offense level of 42 for an offender in criminal history category I).

intended to create a false picture of profitability even for professional analysts that, in Ebbers' case, was motivated by his personal financial circumstances. Given Congress' policy decisions on sentences for fraud, the sentence is harsh but not unreasonable.

CONCLUSION

For the reasons stated, we affirm.

APPENDIX B — ORDER OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK DATED JULY 9, 2005

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

S4 02 Cr. 1144 (BSJ)

UNITED STATES OF AMERICA

v.

BERNARD J. EBBERS,

Defendant

Order

BARBARA S. JONES
UNITED STATES DISTRICT JUDGE

Defendant Bernard J. Ebbers ("Defendant") was charged in a nine-count indictment on March 1, 2004. Count One charged Defendant with conspiracy to commit fraud in connection with the purchase and sale of the securities of WorldCom, Inc. ("WorldCom"), to make and cause to be made false and misleading statements of material fact in various filings with the Securities and Exchange Commission ("SEC"), and to falsify the books, records and accounts of WorldCom. Count Two charged Defendant with securities fraud. Counts Three, Five, Six, Seven and Nine charged Defendant with making false filings with the SEC in WorldCom's Form 10-Qs for the third quarter of 2000, the

first, second and third quarters of 2001 and the first quarter of 2002. Counts Four and Eight charged Defendant with making false filings with the SEC in WorldCom's Form 10-Ks for 2000 and 2001. On March 15, 2005, following a trial that began on January 25, 2005, the jury convicted Defendant of all nine counts.

Defendant now moves for a new trial pursuant to Federal Rule of Criminal Procedure 33, which allows a court to "vacate any judgment and grant a new trial if the interest of justice so requires." Fed. R. Crim. P. 33 (a). Defendant presents three grounds for a new trial: (1) the conscious avoidance jury instruction; (2) rulings regarding certain individuals who did not testify at trial; and (3) rulings on the application of Generally Accepted Accounting Principles ("GAAP") to this case. For the reasons stated below, I find that none of these grounds requires a new trial. Defendant's motion is denied.

I. Background

WorldCom provided a broad range of communications services, including data transmission, commercial voice, international and long distance communications and Internet-related services. WorldCom sold these services to both businesses and individual consumers. The company owned and operated facilities in every major city center in the world and maintained a network of more than 90,000 route miles of land and undersea fiber-optic cable. To serve customers that were not directly connected to that network, WorldCom paid fees to lease network facilities and connections from other telecommunications companies. These fees were known as "line costs" or "Telco costs," and were the company's largest expense.

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At all times relevant to this case, Scott Sullivan served as WorldCom's Chief Financial Officer; Defendant was Chief Executive Officer, President, and a director of the company. In his role as Chief Executive Officer, Defendant provided the investing public with information about WorldCom's financial results and operating performance in a variety of ways, including WorldCom's public filings with the SEC,[1] periodic press releases and company announcements, and statements in meetings, conferences, and conference calls with professional securities any analysts and shareholders.

The information Defendant distributed to investors and analysts included WorldCom's "guidance" regarding the company's financial performance in upcoming quarters. Measures of that performance included the company's cash earnings per share ("EPS"), earnings before interest, taxes, depreciation and amortization ("EBITDA"), net income, expenses, revenue growth, and capital expenditures. Professional securities analysts relied on WorldCom's guidance to make and distribute their own estimates and expectations of the company's future earnings. The investing public, in turn, relied on analysts' earnings estimates in deciding whether to buy, sell or hold WorldCom securities.

Internally, WorldCom tracked its financial performance using a number of different documents, three of which are particularly relevant to this case. The first is a monthly revenue report known as the "MonRev." The MonRev allowed Defendant and other officers and employees to

1. As Chief Executive Officer and President of WorldCom, Defendant was required to sign the Forms 10-K and 10-Q that WorldCom filed with the SEC on an annual and quarterly basis.

review the revenue produced by the company's major sales channels. Revenue not generated in one of those channels was classified as "Corporate Unallocated" revenue. The second relevant report is the Management Budget Variance Report ("MBVR"), which was also produced on a monthly basis. The MBVRs were primarily used to analyze the company's selling, general and administrative costs, or "SG&A" expenses. Each MBVR also contained an executive summary of the company's financial results, including its revenue and line costs. Finally, WorldCom produced preliminary and final income statements on a quarterly basis, which were used to review the company's revenue and expenses.

Starting in September 2000, WorldCom's operating performance and financial results had begun to deteriorate significantly, falling well below both the company's guidance and securities analysts' expectations. To conceal that deterioration, Defendant, Mr. Sullivan and others conspired to make fraudulent adjustments to WorldCom's books and records. Those adjustments centered on two of the company's key financial metrics: line costs and revenue.

The line cost scheme took two different forms. In the third and fourth quarters of 2000, with Defendant's knowledge, Sullivan ordered reductions of line cost expenses by reducing reserve and liability accounts. Those reductions lacked any business justification or supporting documentation.

By March 2001, the company could no longer reduce line costs by debiting reserve and liability accounts because those accounts had been depleted by the entries made in the

third and fourth quarters of 2000. Instead, with Defendant's knowledge, Sullivan ordered employees in the General Accounting Department to transfer line costs from expenses to the company's capital expenditure accounts. This process is known as capitalizing line costs. Under Sullivan's direction, the company capitalized line costs in all four quarters of 2001 and the first quarter of 2002. By reducing reserve accounts and capitalizing line costs, WorldCom fraudulently reduced its reported line cost expenses by more than $500 million per quarter for seven consecutive quarters.

During the same time period, WorldCom increased its reported revenue by recognizing new forms of revenue, solely in order to meet the company's guidance and securities analysts' earnings estimates. Defendant, Sullivan and others at WorldCom created and participated in a process called "Close the Gap" to identify potential adjustments to achieve that goal. Those adjustments were compiled on what were referred to as "hit lists." As a result of that process, WorldCom began to recognize a variety of new forms of revenue, including minimum deficiency penalties,[2] the EDS ratable accrual,[3] and early termination penalties.[4] The new

2. Minimum deficiency penalties are the penalty charges WorldCom was entitled to collect from customers who failed to fulfill their contractual minimum usage requirements.

3. WorldCom had a five-year contract with EDS that contained a minimum usage requirement. The penalty EDS would pay if it did not fulfill that requirement was referred to within WorldCom as the "EDS ratable accrual."

4. Some of WorldCom's customer contracts also permitted the company to collect charges if customers terminated their contracts early. Those charges were referred to as early termination penalties.

revenues from these sources appeared in the Corporate Unallocated line item on the MonRev. These adjustments to WorldCom's revenues marked a departure from the company's prior revenue recognition policies. However, WorldCom did not disclose those changes to the investing public. As a result, its reported revenue was materially misleading.

In furtherance of the scheme to meet the company's guidance and securities analysts' expectations, Defendant falsely described WorldCom's operating performance and financial results to the public, failed to disclose the material facts necessary to make his public statements complete, accurate and not misleading, and caused WorldCom to file financial statements with the SEC that presented false and misleading pictures of the company's operating performance and financial results. The adjustments to line costs and revenues caused all measures of the company's performance, including EBITDA, net income and EPS, to be materially false and misleading. The scheme also caused WorldCom's securities to maintain an artificially high value.

II. Standard on a Rule 33 Motion

Rule 33 permits a trial court "to set aside a jury verdict and order a new trial to avert a perceived miscarriage of justice." *United States v. Sanchez*, 969 F.2d 1409, 1413 (2d Cir. 1992). The ultimate question the court must ask in deciding a Rule 33 motion is whether "it would be a manifest injustice to let the guilty verdict stand." *Id.* at 1414 (quoting *United States v. Reed*, 875 F.2d 107, 114 (7th Cir. 1989)).

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III. Conscious Avoidance

Defendant argues that the jury instruction on conscious avoidance was erroneous, requiring a new trial. I disagree.

A conscious avoidance charge may only be given where two conditions are met: "(1) the defendant asserts the lack of some specific aspect of knowledge required for conviction . . . and (2) the appropriate factual predicate for the charge exists, i.e., 'the evidence is such that a rational juror may reach [the] conclusion beyond a reasonable doubt . . . that [the defendant] was aware of a high probability [of the fact in dispute] and consciously avoided confirming that fact." *United States v. Ferrarini*, 219 F.3d 145, 154 (2d Cir. 2000) (internal citations omitted). The Second Circuit has repeatedly emphasized that it is "essential to the concept of conscious avoidance, that the defendant must be shown to have decided not to learn the key fact, not merely to have failed to learn it through negligence." *United States v. Rodriguez*, 983 F.2d 455, 458 (2d Cir. 1993).

Defendant does not dispute that the first of these conditions was met. Rather, he argues that the factual basis for giving a conscious avoidance charge did not exist here.[5]

5. Defendant also asserts that the conscious avoidance charge was improper because the Government's case proceeded on the theory that Defendant had actual knowledge of the fraudulent scheme at WorldCom. But a conscious avoidance charge is "not inappropriate merely because the government has primarily attempted to prove that the defendant had actual knowledge, while urging in the alternative that if the defendant lacked such knowledge it was only because he had studiously sought to avoid knowing what was plain." *United States v. Hopkins*, 53 F.3d 533, 542 (2d Cir. 1995). Accordingly, Defendant's argument to the contrary is meritless.

Such a basis exists where the "defendant's involvement in the criminal offense may have been *so overwhelmingly suspicious* that the defendant's failure to question the suspicious circumstances establishes the defendant's purposeful contrivance to avoid guilty knowledge." *United States v. Svoboda*, 347 F.3d 471, 480 (2d Cir. 2003) (quoting *United States v. Lara-Velasquez*, 919 F.2d 946, 952 (5th Cir. 1990)).[6]

Defendant contends that the circumstances surrounding his involvement in the fraud at WorldCom were not "overwhelmingly suspicious" enough to justify the conscious avoidance charge. Defendant isolates each piece of evidence

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6. Citing *Ferrarini*, Defendant also argues that the charge was erroneous because "there was only equivocal evidence that [he] . . . had actual knowledge and . . . there was no evidence that [he] . . . deliberately avoided learning the truth." *Ferrarini*, 219 F.3d at 157. In *United States v. Aina-Marshall*, 336 F.3d 167 (2d Cir. 2003), the Second Circuit wrote that "[w]hether this passage even says what [defendant] construes it to mean is doubtful." *Aina-Marshall*, 336 F.3d at 172. The Circuit went on to distinguish the facts of *Ferrarini*, narrowing its applicability to cases where the gravamen of the government's evidence showed the defendant's direct participation in acts that could not have been undertaken without guilty knowledge." *Id.* This is not such a case. The conduct element of the crimes with which Defendant is charged is coterminous with the responsibilities of the Chief Executive Officer position, responsibilities that could have been fulfilled without guilty knowledge of the fraud at WorldCom. Defendant could have spoken with investors, made public statements about WorldCom's financial performance and signed WorldCom's Forms 10-K and 10-Q without knowing about, perpetuating and encouraging the fraudulent scheme. Indeed, it is precisely that scenario that Defendant pressed at trial. *Ferrarini* is accordingly distinguishable from this case.

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I cited in my oral ruling on conscious avoidance and explains how it was not overwhelmingly suspicious. This analysis is problematic for two reasons. First, when I made my ruling, I explicitly stated that I was listing "just a few facts that a rational juror could find" to satisfy the factual predicate for a conscious avoidance change, and that what I cited was "not meant to be an exhaustive list." (Tr. 4104-05.) Second, on a Rule 33 motion, I must "examine the entire case, take into account all facts and circumstances, and make an objective evaluation." *United States* v. *Ferguson*, 246 F.3d 129, 134 (2d Cir. 2001). It is not surprising that, if examined in isolation, no individual piece of evidence is so overwhelmingly suspicious as to justify a conscious avoidance charge. But that is simply not the analysis with which Rule 33 tasks the Court. In fact, when viewed as a whole, the trial record in this case contains abundant proof that. Defendant's involvement in the fraudulent scheme was "so overwhelmingly suspicious" that his "failure to question the suspicious circumstances establishes [his] purposeful contrivance to avoid guilty knowledge." *Svoboda*, 347 F.3d at 480.

The Government showed that between September 2000 and April 2002, Defendant regularly received a variety of financial reports that revealed both WorldCom's deteriorating financial condition and the improper adjustments to line costs and revenue that were made to conceal that deterioration. Defendant received quarterly preliminary income statements that showed WorldCom's actual financial results before the company fraudulently reduced its line costs by between $500 million and nearly $1 billion per quarter for eight consecutive quarters. (Tr. 1867-68.) Defendant received the MBVR on a

monthly basis. (Tr. 4046.) As discussed more fully below, the executive summary of the MBVRs showed WorldCom's monthly line costs over a three month period, thereby exposing the line cost adjustment made in the third month of every quarter. Defendant received both preliminary and final versions of MonRev. (Tr. 1848.) A basic comparison of those documents would have revealed the gross disparity between the company's actual revenue results and the results reported to the public. If indeed Defendant failed to look at a single one of these documents during the eighteen-month-long scheme, it was not due to negligence;[7] it was because he consciously avoided learning the truth behind WorldCom's reported financial performance.

Putting aside the testimony of the four cooperating witnesses, Defendant's own testimony provided the factual predicate for giving the conscious avoidance instruction. Defendant conceded that line costs were the "largest section of expenses" at WorldCom. (Tr. 3713.) Each monthly MBVR, which Defendant testified he received, began with an executive summary, a high-level snapshot of the company's financial results, including the line costs WorldCom incurred each month. The MBVR for the month of September 2000 showed line costs of $732 million; the budget for line costs that month was $1.4 billion, resulting in a discrepancy of

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7. The jury was specifically instructed that "[t]he necessary knowledge on the part of the defendant with respect to Count Two and Counts Three through Nine cannot be established by showing that the defendant was careless, negligent, or foolish. In addition, you may not conclude that the defendant knew of the existence of a particular fact merely because he held the position of chief executive at WorldCom." (Tr. 4444.)

nearly $700 million. When shown this MBVR at trial, Defendant testified that he simply "did not notice that" disparity. (Tr. 4044.) The same page of consolidated results in the September MBVR showed a company-wide gross margin of 78 percent. Defendant agreed "that in the history of WorldCom they never had a margin of 78 percent," but that again, he simply did not notice that figure. (Tr. 4045.)

Defendant justified his failure to see these aberrant numbers based on the fact that he used the MBVRs "exclusively" for reviewing SG&A expenses. (Tr. 4044.) The executive summary, however, included a review of SG&A expenses. Thus according to Defendant's own testimony, he avoided looking at SG&A expenses on a page showing obviously fraudulent line cost figures, to focus instead on the voluminous, minutely detailed pages supporting that summary. This explanation only makes his review of the MBVRs more "overwhelmingly suspicious."

Defendant gave almost identical testimony regarding the MBVR for the month of December 2000. Like the September MBVR, the first pages in the December MBVR showed the company's consolidated financial results, including SG&A expenses, the very expenses on which Defendant testified he focused. The December report showed a line cost entry of $856 million and a budgeted amount of $1.5 billion, producing a variance of about $654 million. (Tr. 4049.) Defendant testified that he was familiar with "the general range of what line costs were for WorldCom on a monthly basis," and that "40 percent was about the percentage" of revenue that management of WorldCom expected line costs

to be. (Tr. 4049.) The December MBVR, however, showed line costs of 26 percent of revenue. Defendant conceded that the 26 percent figure was "nowhere close" to accurate. (Tr. 4049.) The Government then asked Defendant a series of questions about the apparent suspiciousness of these figures, and received the following responses:

Q: It's clear from the page that there is an adjustment that was made to line costs, correct?

A: There appears to be, yes.

Q: There is no other conclusion you could reach from seeing a line cost to revenue ratio of 26 percent, correct?

A: If you had seen it, you sure would ask questions.

Q: At a minimum. And I take it your testimony is you just didn't see it.

A: I just didn't see it.

(Tr. 4049-50.)

The irregularity of the line cost figure for December 2000 was made more apparent by the MBVR for January 2001. That report showed line costs of $1.5 billion for October 2000, $1.6 billion for November 2000, and $858 million for December 2000. In January 2001, line costs rose back to $1.6 billion. When Defendant was asked, "it's obvious from looking at this document that there is an adjustment made in December 2000, isn't there?" he responded, "Something's

been done." (Tr. 4058.) Again, however, he testified that he "just did not look at it." (Tr. 4053.)

Defendant testified that in February 2001, the same month the January 2001 MBVR was distributed, he attended a dinner with Scott Sullivan, Ron Beaumont and Tom Bosley. Defendant said that at that dinner, "the comment was made that we need to do everything we can to put in programs to lower line costs." (Tr. 4054.) The Government then asked "Because they were running too high?," and Defendant responded, "They were not coming down as fast as we thought they should." (Tr. 4054.)

The MBVR for March 2001 — produced one month after Defendant admits he had a conversation about WorldCom's rising line costs — showed the same aberrant trend as did the September 2000, December 2000 and January 2001 MBVRs. The consolidated company-wide results showed line costs of $1.6 billion for January 2001, $1.6 billion for February 2001, and $809 million for March 2001. When the Government asked "There is plainly an adjustment to those numbers, correct?," Defendant agreed. (Tr. 4057-58.) But despite the discussions he admits to having with his fellow officers about the company's problem with line costs, he testified that starting in 2001, when MBVRs no longer included the company's budget numbers, he probably put the reports "in the trash." (Tr. 4058.) Nonetheless, Defendant admitted that he never requested that the accounting group stop sending the MBVRs to him. (Tr. 4058.)

Defendant testified that he attended quarterly line cost meetings beginning in the second quarter of 2001. He

admitted that at the June 2001 line cost meeting, he knew that line costs "were not coming down as expected." (Tr. 4063.)

Defendant testified that he attended a February 2002 meeting with Scott Sullivan, Ron Beaumont, Scott Hamilton and Blair Bingham, at which a graph was presented showing what maintenance capital expenditures should be at various levels of revenue growth. (Tr. 4065.) The graph showed that for five percent revenue growth, WorldCom would be expected to spend $3 billion on maintenance capital. In that same month, WorldCom's earnings press release predicted that the company would have "mid single digit revenue growth," which Defendant conceded would be in the range of four to six percent revenue growth. (Tr 4067.) However, WorldCom announced that its capital expenditures would be between $5 and $5.5 billion. (Tr. 4066-67.) Defendant admitted that this capital expenditures figure represents a $2 billion variance over what the graph showed would be appropriate for mid single digit revenue growth. Defendant testified that Scott Sullivan explained the $2 billion disparity based on "items like Embratel, Avantel, the other subsidiaries that we had, they required some capital, software system development that was corporate related, things like that, capitalized labor." (Tr. 4067-68.) But Defendant admitted that Sullivan's explanation for the disparity between the figures was incomplete.[8] (Tr. 4068.)

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8. Scott Sullivan testified that the gap between the figures was due to line cost capitalization. He thus explained:

> 43 billion is the amount of capital that you would spend for 5 percent revenue growth, the real amount of capital

(Cont'd)

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As he did for the adjustments made in the third and fourth quarters of 2000 and the first quarter of 2001, Defendant professed ignorance of the fraudulent entries made for the rest of 2001. Defendant testified that he knew nothing about the adjustments that reduced line costs by $610 million in the second quarter of 2001, by $742 million in the third quarter of 2001, and by $941 million in the fourth quarter of 2001. (Tr. 4053.) Defendant admitted that WorldCom fraudulently reduced its line costs by over $2 billion, but claimed he had no idea it had done so. (Tr. 4063.) Finally, Defendant conceded that those reductions in line costs would impact all key measures of WorldCom's financial performance, including its net income, EPS and EBITDA. (Tr. 4058.) He agreed that such adjustments would make all those figures artificially high. (Tr. 4058.)

This testimony provides a more than adequate factual basis for a conscious avoidance charge. Defendant knew that line costs were the company's largest expense and that those costs were rising. He received and reviewed MBVRs in the third and fourth quarters of 2000, but he never looked at the pages showing the company's consolidated results, despite

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(Cont'd)

> that you would spend for equipment, fiberoptics, switches, the things that you need to do to invest in the business in order to grow at a 5 percent revenue growth rate. The higher amount of capital expenditures, $5.5 billion, includes line cost expenses that have been added in to the capital expenditure number that's reported to the public.

(Tr. 2418.)

the fact that those results included SG&A expenses, the very expenses on which Defendant claims he focused. Defendant admitted that an artificial reduction of line costs would cause all of WorldCom's financial results to be fraudulently high. Yet given these circumstances, Defendant claimed he knew nothing of the more than $2 billion in fraudulent line cost reductions made between September 2000 and April 2002. Taken as a whole, this testimony, all from Defendant himself, would permit a rational juror to find that Defendant's involvement in the fraud at WorldCom was so overwhelmingly suspicious that his ignorance was due to his conscious avoidance of guilty knowledge. I therefore find that the conscious avoidance instruction was proper. Defendant's motion for a new trial on that basis is denied.

IV. Rulings Regarding Ronald Beaumont, Ronald Lomenzo and Stephanie Scott

Defendant next focuses on three individuals: Ronald Beaumont, who served as Chief Operating Officer of WorldCom; Ronald Lomenzo, who was the company's Senior Vice President of Revenue Accounting; and Stephanie Scott, former Vice President of Financial Reporting. Defendant argues that various rulings concerning these individuals deprived him of a fair trial. These arguments lack merit.

The Government interviewed many former WorldCom employees during its investigation of this case, including Beaumont, Lomenzo and Scott. As a result of its investigation, the Government has thus far brought charges against six former WorldCom employees: Defendant, Scott Sullivan, David Myers, Buford Yates, Betty Vinson and Troy Normand. The latter five

individuals pleaded guilty and agreed to cooperate with the Government in its case against Defendant in exchange for the Government's agreement not to prosecute them further. The Government entered into non-prosecution agreements with two other individuals and obtained an order of use immunity for a third individual, Lisa Taranto, who testified at trial. Although it has interviewed Beaumont, Lomenzo and Scott, the Government has not brought any charges against them, nor has it granted them immunity. The Government identified all three individuals as unindicted co-conspirators.

At trial, Defendant subpoenaed Beaumont, Lomenzo and Scott. All three notified him, through their counsel, that they would invoke their Fifth Amendment rights against self-incrimination if he called them to testify.

Defendant's Rule 33 motion attacks three sets of rulings that dealt with Beaumont, Lomenzo and Scott. The first ruling denied Defendant's application for court-ordered immunity for these three potential defense witnesses. Before trial, Defendant moved for the Court to compel the Government to grant immunity to Beaumont and Lomenzo, which was denied in a written order dated November 10, 2004. At the close of the Government's case, Defendant again moved the court to compel defense witness immunity for Beaumont and Lomenzo, as well as Stephanie Scott. I again denied the motion.

The second set of rulings applied to Defendant's motion, brought under Federal Rule of Civil Procedure 806, to impeach the hearsay declarations of Beaumont, Lomenzo and Scott introduced at trial using five of their prior statements.

I permitted the introduction of one of those statements, but denied the motions as to the other four.

The third ruling Defendant attacks is the denial of his request that I give the jury a "missing witness" instruction.

Finally, Defendant argues that a new trial is necessary due to certain statements the Government made during its summation. I instructed the jury to disregard those remarks, but Defendant nonetheless argues that they caused him incurable prejudice. I will address each of these arguments in turn.

A. Defense Witness Immunity

"Immunity remains 'pre-eminently a function of the Executive Branch.'" *United States v. Salerno*, 937 F.2d 797, 807 (2d Cir. 1991). There exist "substantial risks to potential future prosecutions inherent in grants of use immunity." *United States v. Todaro*, 744 F.2d 5, 9 (2d Cir. 1984). Courts in this Circuit thus do not order the government to grant defense witness immunity, but rather use a "carrot-and-stick approach, leaving the immunity decision to the executive branch but interposing the judicial power to subject the government to certain choices of action," generally between granting immunity and facing dismissal of the indictment. *United States v. Bahadar*, 954 F.2d 821, 826 (2d. Cir. 1992). This course of action is appropriate only where three conditions are met:

> First, the district court must find that the government has engaged in discriminatory use of

> immunity to gain a tactical advantage or, through its own overreaching, has forced the witness to invoke the fifth amendment. Second, the witness's testimony must be "material, exculpatory, and not cumulative". Third, the testimony must be unobtainable from any other source.

United States v. Bahadar, 954 F.2d 821, 826 (2d. Cir. 1992) (citing *United States v. Burns*, 684 F.2d 1066, 1077 (2d Cir. 1962), *cert. denied*, 459 U.S. 1174 (1983)).

The Second Circuit has advised that "trial judges should summarily reject claims for defense witness immunity whenever the witness for whom immunity is sought is an actual or potential target of prosecution. No hearing should be held to establish such status." *United States v. Turkish*, 623 F.2d 769, 778 (2d Cir. 1980). Eight years after it decided *Burns*, the Second Circuit had yet "to be presented with a case in which the defendant gets over the first hurdle, let alone succeeds entirely." *Bahadar*, 954 F.2d at 826. I am aware of no such case to this day. *See, e.g., United States v. Karlsen*, No. S4 00 Cr. 502 (JSM), 2001 WL 428246, at *1 (S.D.N.Y. Apr. 26, 2001).

As to the first hurdle, Defendant argues that "the only conclusion that can be drawn from the government's refusal to decline prosecution of, or grant immunity to, [Beaumont, Lomenzo and Scott] is that the government did so for tactical reasons to ensure that these exculpatory witnesses would be unavailable to [his] defense." (D. Mot. at 33-34.) Defendant contends that he was "the CEO of WorldCom and the principal target of the government's investigation from its

inception." (D. Mot. at 33.) As a result, the Government "cannot credibly maintain that it was awaiting the outcome of [Defendant's] trial to decide whether to prosecute Messrs. Beaumont and Lomenzo and Ms. Scott." (D. Mot. at 33.)

That contention is without merit. Following the practice outlined in *Turkish*, the Government has presented "*in camera* an *ex parte* affidavit setting forth the circumstances that support [its] suspicion of the witness's criminal activity," thereby demonstrating that it has not used immunity to gain a tactical advantage. *Turkish*, 623 F.2d at 778. Furthermore, that the Government has chosen to immunize some individuals but not others does not prove a violation of Defendant's constitutional rights; that choice is "an every day occurrence in criminal prosecutions." *Karlsen*, 2001 WL 428246 at *1. There is simply no proof on the record that the Government has used immunity tactically. Without more, Defendant cannot overcome the first hurdle of the *Burns* test.

Although it is unnecessary to do so, I also find that Defendant fails to satisfy the second element of the *Burns* test. As proffered by Defendant, the testimony of Beaumont, Lomenzo and Scott would not be exculpatory. Instead, they each "would have testified that they were unaware of the fraud committed by Scott Sullivan and his staff despite its magnitude," thereby exculpating themselves from the fraud. (D. Mot. at 35.) That these individuals did not know about the fraud at WorldCom does not prove that Defendant was similarly ignorant. There is no evidence that they saw the same documents as Defendant, or were in any other way similarly situated to him. Defendant's "overall involvement" in the fraudulent scheme therefore "could not have been

rebutted by" their testimony. *United States v. Chitty*, 760 F.2d 425, 429-30 (2d Cir. 1985).

It is also worth noting that a number of other witnesses, including Scott Hamilton, Brady Connor and Cynthia Cooper, professed ignorance of the fraudulent scheme. Yet Defendant does not argue that their lack of knowledge proves his innocence. These witnesses' testimony further shows that, contrary to Defendant's argument, the Government did not portray WorldCom as a criminal enterprise.

Defendant also argues that the testimony of Beaumont, Lomenzo and Scott would have impeached Scott Sullivan and David Myers. But even assuming that the "exculpatory evidence" prong of *Burns* includes impeachment evidence,[9] no such evidence is to be gained from these individuals' testimony. *See* Section IV(B), *infra*.

In conclusion, Defendant fails to show that the Government has used immunity to gain a tactical advantage over him, or that the testimony of Beaumont, Lomenzo or Scott would be exculpatory. Defendant's motion for a new trial on this basis is therefore denied.

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9. It is not at all clear that "exculpatory" under *Burns* includes impeachment evidence. Under *Brady*, the term "favorable" evidence is used to encompass evidence that either "tends to exculpate the accused" or "is useful to impeach the credibility of a government witness." *In re United States* (*Coppa*, 267 F.3d 132, 139 (2d Cir. 2001). But no court has indicated, much less held, that "exculpatory," as used in *Burns*, has the same broad meaning that "favorable" does under *Brady*. In fact, *United States v. Chitty*, 760 F.2d 425 (2d Cir. 1985), supports a contrary reading.

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B. Impeachment of Hearsay Declarants

Defendant next moves to impeach, under Federal Rule of Evidence 806, the hearsay declarations of Beaumont, Lomenzo and Scott, as reported at trial by David Myers and Scott Sullivan. I find that the prior inconsistent statements at issue were properly precluded, and therefore my previous rulings do not justify a new trial.

Rule 806 provides in relevant part: "When a hearsay statement . . . has been admitted in evidence, the credibility of the declarant may be attacked . . . by any evidence which would be admissible for those purposes if declarant had testified as a witness." Fed. R. Evid. 806. Rule 806 thus "simply makes an otherwise hearsay statement admissible when the Declarant (co-conspirator) has not taken the stand, but his statements have nevertheless come into evidence as a statement in furtherance of the conspiracy." *United States v. Rosario*, 111 F.3d 293, 296 (2d Cir. 1997). "A party is allowed no greater latitude in impeaching a hearsay declarant pursuant to Rule 806, than the party would otherwise be permitted by the rules of evidence in impeaching a witness that testified at trial." *United States v. Mejia-Velez*, 855 F. Supp. 607, 615 (2d Cir. 1994).

Before admitting a statement under Rule 806, the court must "first decide whether the proffered statement is actually inconsistent with the hearsay statement already admitted." *United States v. Graham*, 858 F.2d 986, 990 (5th Cir. 1988). To serve as impeachment material, the two statements "need not be diametrically opposed," but they must nonetheless be inconsistent with one another. *United States v. Agajanian*,

852 F.2d 56, 58 (2d Cir. 1988). Second, the court must confirm that the proffered statement will be admitted for impeachment, not for its truth. *See Melia-Velez*, 855 F. Supp. at 616 (rejecting the statement proffered by the defendant because it was "not offered for a proper impeachment purpose").

Defendant first proffered the statement, made by Mr. Beaumont in an interview with the Government, that he "was not involved in the release of reserves in the third quarter of the year 2000," and that the only reserve he was "ever involved in" was in 2001. (GX 3534A at 7.) Defendant argues that this statement would impeach Beaumont's declaration in February 2001 that, "we don't have reserves to take like we did last year, Tom, so we've got some real cutting to do in that area." (Tr. 2066-67.) Scott Sullivan reported this hearsay statement.

These statements do not contradict each other. Beaumont could have been uninvolved in the releases of reserves in the third and fourth quarters of 2000 and nonetheless have known by February 2001 that WorldCom no longer had "reserves to take like [it] did last year." (Tr. 2066-67.)

In fact, when read in its proper context, Beaumont's prior statement to the Government is entirely consistent with his hearsay declaration introduced at trial. In the same proffer session in which Beaumont denied any involvement in the reserve releases in the third and fourth quarters of 2000, Beaumont said that in early 2001 he told David Myers that "no reserves would be tapped in this early 2001 period because there were none." (GX 3534A at 7.) Beaumont thus

conceded that, as of early 2001, he knew that WorldCom's reserve accounts had been depleted. The statement Sullivan attributed to him at trial was, in substance, identical.

Defendant's next area of proposed impeachment dealt with the removal of Beaumont's Close the Gap slides from his presentations to the WorldCom Board of Directors. Those slides were included Beaumont's June 2001 presentation but were missing from his September 2001 presentation. Scott Sullivan testified that Defendant told Beaumont, in Sullivan's presence, "not to get into [C]lose the [G]ap items for the third quarter of 2001," and that Beaumont complied. (Tr. 2342-43.) Under the guise of impeaching Beaumont, Defendant moved to introduce Beaumont's statement to the Government that no one told him to remove the Close the Gap slides from his board presentation. Defendant argues that this statement would impeach Beaumont's "alleged silence in the face of Mr. Ebbers' alleged order," which Defendant labels a "hearsay assertion" in the form of nonverbal conduct. (D. Mot. at 38.)

Although nonverbal conduct can be a statement "if it is intended by the person as an assertion," there is nothing in the record to indicate that Beaumont intended, through his silent removal of the Close the Gap slides, to assert that Defendant commanded him to remove them. *United States v. Aspinall*, 389 F.3d 332, 342 (2d Cir. 2004). As a result, there is simply no statement of Beaumont for Defendant to impeach. This portion of Defendant's motion was clearly an effort to impeach Sullivan, not Beaumont.

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Defendant's third proposed area of impeachment was a hearsay statement of Beaumont, reported by Sullivan, made during a February 6, 2002 meeting between Defendant, Hamilton, Beaumont and Sullivan. Sullivan testified that at that meeting, Beaumont drew a graph showing the ratio of WorldCom's revenue to its capital expenditures. The graph revealed that at five percent revenue growth, WorldCom should spend approximately $3 billion in maintenance capital expenditures. Yet in February 2002, when WorldCom announced mid single digit revenue growth, it reported capital expenditures of between $5 and $5.5 billion. This figure represents a $2 to $2.5 billion disparity between what WorldCom's capital expenditures should have been and what the company reported to the public.

Sullivan testified that after drawing the graph, Beaumont declared, "Bernie, we are already at $3 billion and below. Our people are already there. The rest of the number, it's all Scott's stuff." (Tr. 2418.) Sullivan testified that his understanding of what Beaumont meant by "Scott's stuff" was "the line cost expenses that I was putting into our capital expenditures number." (Tr. 2418-19.) Defendant proposed to impeach this testimony with Beaumont's statement, at an interview with the Government, that he believed the disparity between the two capital expenditure figures was due to "Scott's cushion for cash" and "was never tied to capitalized line costs." (GX 3534B at 2.)

This proposed line of impeachment suffers two fatal flaws. First, the statement Sullivan attributes to Beaumont regarding "Scott's stuff" is not inconsistent with Beaumont's later statement to the Government about "Scott's cushion

for cash." Second, Defendant aims to impeach Sullivan's interpretation of Beaumont's statement, not the statement itself. But that is not proper impeachment under Rule 806. *See Graham*, 858 F.2d 986, 990 ("rule 806, which establishes standards only for the impeachment of [a hearsay declarant], does not authorize introduction of . . . subsequent hearsay statements impeaching" the witness who reported the original hearsay).

The final Rule 806 issue deals with Lisa Taranto's testimony that Stephanie Scott ordered her to create a "special" MonRev report because as Ms. Scott explained to her, she "wanted to minimize the amount of revenue items that were corporate unallocated for her presentation to Arthur Anderson." (Tr. 3054.) Defendant proposed to impeach this hearsay with Ms. Scott's denial, in her interview with the Government, of knowing about a special MonRev. This impeachment would be improper because there was no hearsay statement for Defendant to impeach; Ms. Scott's commands "were not offered to prove the truth of the statements contained within them, but instead to prove the fact that certain instructions had been given." *United States v. Reilly*, 33 F.3d 1396, 1410 (3d Cir. 1994). Again, it seems clear that Defendant aims only to impeach Taranto, not Scott.

In conclusion, none of the four statements Defendant proffered were proper impeachment under Rule 806. Accordingly, his motion for a new trial on those grounds is denied.

Appendix B

C. The Missing Witness Instruction

Defendant requested that I give a missing witness instruction due to the Government's refusal to immunize Beaumont, Lomenzo and Scott.[10] I declined to do so. Defendant now argues that this ruling was in error because under "circumstances that indicate the [G]overnment has failed to immunize an exculpatory witness," the court must give a missing witness instruction. *Myerson*, 18 F.3d at 160.[11] I disagree.

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10. Defendant's proposed instruction was entitled "Uncalled Witness Not Equally Available to Defendant" and provided:

> You have heard evidence about a number of witnesses who have not been called to testify. The defense has argued that the witnesses could have given material testimony in this case and that the government was in the best position to produce these witnesses.
>
> If you find that these uncalled witnesses could have been called by the government and would have given important new testimony, and that the government was in the best position to call them, but failed to do so, you are permitted, but you are not required, to infer that the testimony of the uncalled witnesses would have been unfavorable to the government.
>
> In deciding whether to draw an inference that the uncalled witnesses would have testified unfavorably to the government, you may consider whether the witnesses' testimony would have merely repeated other testimony and evidence already before you.

11. Defendant misreads *Myerson*. The Second Circuit held there that "in the absence of circumstances that indicate the government has failed to immunize an exculpatory witness, a district court does

(Cont'd)

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The relevant inquiry for a missing witness charge is not whether the witness would be exculpatory,[12] but rather whether the witness is available to one side rather than the other. A missing witness instruction thus may be appropriate where one party "has it particularly within his power to produce witnesses" yet chooses not to do so. *Sagendorf-Teal v. County* of *Rensselaer*, 100 F.3d 270, 275 (2d Cir. 1995). Under those circumstances, the "jury may infer that 'the testimony, if produced, would be unfavorable' to that party" who failed to call the witness. *United States v. Torres*, 845 F.2d 1165, 1169 (2d Cir. 1988) (quoting *Graves v. United States*, 150 U.S. 118, 121, 14 S. Ct . 40, 41 (1893)). But the jury should draw no such inference where the "witness is equally available to both sides." *Id.*

A proposed defense witness who invokes his or her Fifth Amendment right not to testify is equally unavailable to both the government and the defense, even if the government could have hypothetically granted immunity. Thus in *Myerson*, the Second Circuit observed:

> [i]n refusing to require that a missing witness charge be given in each instance that a witness

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(Cont'd)

not abuse its discretion by refusing to give a missing witness charge." *Myerson*, 18 F.3d at 160. This statement is not the equivalent of holding that the Government's failure to immunize an exculpatory witness in every case requires that a missing witness charge be given.

12. Even if Defendant were correct in his statement of the law, as I noted in Section: IV(A), *supra*, the testimony of Beaumont, Lomenzo and Scott would not exculpate him.

> asserts his Fifth Amendment privilege, appellate courts have recognized that such a requirement would unnecessarily infringe on the prosecutorial decision of whether or not to grant immunity ... Moreover, a prosecutor's failure to immunize a witness does not, categorically, give rise to an inference that that the witness's testimony would be unfavorable to the government.

Myerson, 18 F.3d at 159. The court also noted that "[o]ther circuits to consider the issue are unanimous . . . in holding that, despite the government's power to grant immunity, a witness invoking his constitutional rights is unavailable to the government as well as the defense, and no missing witness charge need be given." *Id.* at 169.

Accordingly, the fact that Beaumont, Lomenzo and Scott refused to testify made them unavailable to both the Government and Defendant, thus precluding the jury from inferring that their testimony would be unfavorable to the Government. It follows that permitting Defendant to argue that inference would have been improper. Defendant's motion for a new trial on this basis is denied.

D. Government Summation

Defendant asserts that the Government "improperly vouched for the credibility of its cooperating witnesses during summation by implying that their testimony had been corroborated by evidence outside the record." (D. Mot. at 44.) Defendant further argues that the jury could have inferred that such improper corroboration came from Beaumont,

Lomenzo and Scott, all of whom "had directly contradicted the testimony of the cooperating witnesses," but about whose absence Defendant was precluded from arguing. (D. Mot. at 47.) Although I gave a curative instruction after the Government made the challenged statements, Defendant nonetheless claims that "the prejudice was incapable of being cured where the credibility of the government's cooperating witnesses was the critical issue on which guilt or innocence turned." (D. Mot. at 44.)

During its summation, the Government defended the credibility of its cooperating witnesses with the following statement:

> They are guaranteed not to get a reduced sentence if they lie in court. These witnesses have known from the beginning that there are other people out there who the Government can talk to to confirm whether they are telling the truth. These witnesses know that there is other evidence out there to confirm whether they are telling the truth. If they lie, they will get exposed.

(Tr. 4233.) The Government completed its summation soon after that, and defense counsel then objected at a sidebar conference. (Tr. 4244-48.) I agreed to strike the argument because I found that it was "susceptible to two different interpretations," one being that there was evidence beyond the evidence introduced at trial that corroborated the Government's cooperating witnesses. (Tr. 4247.) I then instructed the jury to disregard the prosecutor's statement. (Tr. 4248-49.)

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The standards for granting a new trial based on a statement in the Government's summation are quite stringent: "a prosecutor's comments upon summation must 'so infect [] the trial with unfairness as to make the resulting conviction a denial of due process.'" *United States v. Coriaty*, 300 F.3d 244, 255 (2d Cir. 2002) (quoting *Donnelly v. DeChristoforo*, 416 U.S. 637, 643, 94 S. Ct. 1868, 1871 (1974)). In particular, a defendant must show "(1) that the prosecutor's statements were improper and (2) that the remarks, taken in the context of the entire trial, resulted in substantial prejudice." *United States v. Thomas*, 377 F.3d 232, 244 (2d Cir. 2004) (quoting *United States v. Perez*, 144 F.3d 204, 210 (2d Cir. 1998)). As to the second element, three factors determine whether the Government caused the defendant substantial prejudice: "the severity of the misconduct; the measures adopted to cure the misconduct; and the certainty of conviction absent the improper statements." *Id.* at 245. In this case, if interpreted as a reference to extra-record evidence, of course the Government's comments in summation would be improper. I also find, however, that even if so interpreted, they caused Defendant no substantial prejudice. Indeed, all three factors weigh against such a finding.

First, the Government's statement does not amount to misconduct. It was quite clear from the prosecutor's protestations at sidebar, which I credit, that he did not intend to draw the jury's attention to evidence outside the record, but rather to the Government's other cooperating witnesses and the documents introduced at trial. (Tr. 4246-47.) Unfortunately, he used ambiguous language to do so, which, while not a laudable trial advocacy technique, hardly constitutes misconduct, let alone severe misconduct.

Additionally, these comments were but "minor aberrations"; they lasted no more than a few seconds in the midst of a nearly four hour summation at the close of a six week trial. *United States v. Socony-Vacuum Oil Co.*, 310 U.S. 150, 240, 60 S. Ct. 811, 852 (1940). The remainder of the trial was certainly not "a proceeding dominated by passion and prejudice." *Id.* at 240. Indeed, Defendant does not challenge the Government's opening statement or, for that matter, any of the Government's other conduct throughout the trial. *See, e.g., Thomas*, 377 F.3d at 245.

Second, I gave the jury a curative instruction immediately following the Government's summation, only minutes after the comments were made. A remedy could have come no sooner, for the defense failed to raise the issue until after the Government completed its summation. (Tr. 4246.) In my instruction, I referenced the Government's ambiguous statement and instructed the jury to disregard it entirely. (Tr. 4248-4249.)

Third, it is extremely likely that the jury would have convicted Defendant even if the Government had not made the remarks in question. The proof against Defendant was strong. Four cooperating witnesses outlined the fraud in painstaking detail. Defendant's personal role in the scheme, as an instigator and participant, was described by Scott Sullivan and supported by the numerous documents the Government introduced at trial and showed that Defendant received. Considering the heft of this evidence, it is extraordinarily unlikely that one oblique comment by the Government at the end of a lengthy, detailed summation could have made any difference in the jury's ultimate decision to convict. Defendant's motion for a new trial on these grounds is therefore denied.

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V. GAAP

Defendant argues that a new trial is warranted based on three rulings that dealt with GAAP. First, he alleges that the Government was required, and failed, to prove that the accounting decisions at issue in this case violated GAAP. Second, Defendant contends that it was error not to give his proposed jury instruction regarding GAAP. Finally, Defendant argues that he should have been permitted to use certain exhibits as substantive evidence that WorldCom's accounting decisions complied with GAAP. None of these grounds requires a new trial.

A. Proof of a GAAP Violation

Defendant has repeatedly pressed the view that proof of a GAAP violation was required for his conviction of conspiracy to commit securities fraud, securities fraud, and causing false filings to be made with the SEC. Defendant moved before trial to dismiss the Indictment because it failed to allege that the fraudulent entries violated GAAP. At the close of the Government's case, Defendant moved to dismiss the case based on the the Government's failure to prove a GAAP violation. I denied both motions, for the same reason I deny the instant motion: a GAAP violation is not an element of any of the crimes charged in the Indictment. *See, e.g., United States v. Simon*, 425 F.2d 796, 805 (2d Cir. 1969). The Government is not required to prove such a violation beyond a reasonable doubt in order for Defendant to be convicted. Accordingly, Defendant's motion for a new trial on this basis is denied.

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B. Jury Instructions on GAAP

Defendant argues that it was error not to instruct the jury that WorldCom's compliance with GAAP could serve as evidence that his statements about WorldCom's revenue accounting[13] were not materially false and misleading.[14] I have reviewed the trial record of this case and can find no foundation whatsoever for this instruction. Defendant's motion for a new trial on this basis is therefore denied.[15]

Defendant contends that his proposed instruction would have been appropriate in this case because there was "some

13. Defendant never argued that GAAP could provide a substantive defense to the line cost capitalization scheme.

14. Defendant's GAAP instruction was part of his proposed instruction on the first element of securities fraud, and provided:

> In determining whether statements regarding WorldCom's financial results contained material misstatements or omitted material facts, you may consider whether WorldCom's financial statements or the accounting transactions upon which they were based complied with Generally Accepted Accounting Principles. Evidence that the financial statements or accounting transactions at issue complied with Generally Accepted Accounting Principles is very persuasive but not necessarily conclusive evidence that the statements regarding WorldCom's financial results were not materially false and misleading.

15. In his motion for a new trial, Defendant also argues that it was error not to instruct the jury that Defendant's receipt of information indicating that WorldCom's financial statements complied with GAAP could serve as evidence of Defendant's good faith. In support of this argument, Defendant cites *United States v. Simon*, 425 F.2d 796 (2d Cir. 1969), as lending support for a good faith charge based on GAAP compliance. However, I gave the instruction Defendant proposed. (Tr. 4470.) This argument is accordingly moot.

foundation in the proof" introduced at trial that WorldCom's revenue accounting complied with GAAP. *United States v. Dove*, 916 F.2d 41, 47 (2d Cir. 1990). Defendant identifies three pieces of evidence that he argues, if taken together, would support his proposed jury charge. First, Defendant points to Arthur Andersen's audit opinions for 2000 and 2001, in which Andersen found that WorldCom's financial statements complied with GAAP. (Tr. 3359.) The audit opinions were admitted through Cynthia Cooper, who served as WorldCom's Chief Audit Executive during the relevant time period. Second, Defendant highlights WorldCom's Form 10-Ks for 2000 and 2001, in which Andersen represented that the forms' financial statements complied with GAAP. Finally, Defendant calls attention to Lisa Taranto's testimony that WorldCom disclosed the details of two new forms of revenue, minimum deficiencies and the EDS ratable accrual, to Arthur Andersen. Defendant thus argues that because Arthur Andersen was notified of these items and nonetheless issued audit opinions that WorldCom's financial statements complied with GAAP, WorldCom's revenue accounting complied with GAAP, thereby providing "some foundation" for Defendant's proposed GAAP instruction.

Although this argument may have superficial appeal, particularly in light of the standard set out in *Dove*, the trial record in fact contains no proof whatsoever that WorldCom's financial statements, including its revenue accounting, complied with GAAP. Examination of the three pieces of evidence on which Defendant focuses makes this abundantly clear.

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First, Ms. Taranto's testimony does not support the proposition that Arthur Andersen's clean audit opinions were based on full and complete information. Rather, Ms. Taranto testified that in the third quarter of 2000, Stephanie Scott asked her to create a special MonRev for Arthur Andersen. To create the special MonRev, Ms. Taranto moved over $175 million in revenues from the Corporate Unallocated line item to various sales channels. (Tr. 3054.) Ms. Taranto explained that those items did not belong in sales channels because they were not tied to the company's operational performance. (Tr. 3054-55.) In fact, she simply spread the Corporate Unallocated figure proportionately among WorldCom's different sales regions. (Tr. 3054.) She thus explained: "If a certain sales region in major nationals had, for example, 10 percent of the total revenue, then I would allocate 10 percent of the credits to that region." (Tr 3061.) She was given no documentation to support this reallocation. (Tr. 3061.) Included in the reallocation was the revenue WorldCom recognized based on the EDS ratable accrual. (T: 3062.) Thus the EDS ratable accrual — which Defendant claims was disclosed to Arthur Andersen — was in fact hidden from the auditor in the special MonRev.

Ms. Taranto further testified about her failure to disclose a number of WorldCom's other revenue accounting decisions between September 2000 and June 2002. She testified that she neither told Arthur Andersen about the hit lists that she and Ron Lomenzo created to meet WorldCom's revenue guidance, nor gave Andersen any of those hit lists. (Tr. 3082.) Similarly, she never spoke with anyone at Arthur Andersen about the Close the Gap process, and did not give any of the Close the Gap schedules to Arthur Andersen. (Tr. 3082.)

Ms. Taranto did testify that sometime in October 2000, she informed Arthur Andersen that WorldCom had changed its accounting treatment of minimum deficiencies. (Tr. 3015-16.) Whereas before that time WorldCom did not recognize minimum deficiencies as revenue until the customer actually paid those charges, after October 2000, the company recorded as revenue charges that had not yet been collected from its customers. (Tr. 3015.) However, Ms. Taranto never identified the minimum deficiencies entry she made in October 2000 to adjust WorldCom's September 2000 financial results, whereby the company moved $133 million of its minimum deficiencies reserves from its balance sheet to the revenue line of its income statement. (Tr. 3016.) Nor did she inform Arthur Andersen that one of the reasons WorldCom changed its treatment of minimum deficiencies was in order to meet securities analysts' earnings expectations for the company. (Tr. 3022.)

Ms. Taranto's testimony thus shows that when Arthur Andersen issued its audit opinions in 2000 and 2001 and its representations in the company's Form 10-Ks for those years, it did so based on incomplete information. Facts surrounding the EDS ratable accrual, minimum deficiencies and Close the Gap were either not disclosed to, or were affirmatively concealed from, Andersen. The combination of Ms. Taranto's testimony and Andersen's audit opinions thus provides no foundation for the claim that WorldCom's revenue accounting complied with GAAP.

An additional problem plagues Defendant's argument: the Arthur Andersen audit opinions were not admitted for the truth of what they asserted, but rather as evidence of

Defendant's state of mind. When determining the potential use of these documents, I specifically asked defense counsel, "If you have somebody who will come in here and say they reviewed all of this and they thought that accounting was legitimate and you have a defense to the actual substantive fraud, who are those people?" (Tr. 3165.) Defense counsel responded that Ken Avery, the head of the Arthur Andersen team at WorldCom, would fill that role. Indeed, defense counsel conceded that the delivery of the audit opinions to Defendant was "half the puzzle. The other has to come from Avery." (Tr. 3166.) Defense counsel explained that "when coupled with additional evidence we hope to offer through Ken Avery that they reviewed specific transactions .. . that is objective evidence that the accounting on the revenue side was legitimate." (Tr. 3167.) But neither Mr. Avery, nor any other Arthur Andersen employee, testified at trial. Alternatively, no expert witness testified to finding that, having examined the books and records of the company, its financial statements complied with GAAP. Thus based on Defendant's own proffer, the Andersen audit opinions could not serve as substantive evidence of WorldCom's compliance with GAAP.

In fact, GAAP played no role in this trial whatsoever. Not a single witness, for either Defendant or the Government, testified about the substance of GAAP or its application to WorldCom. Beyond an early explanation of what the acronym "GAAP" stands for and a few vague descriptions of the difference between GAAP and cash accounting, GAAP was barely even mentioned at trial. There was simply no foundation for a jury instruction about WorldCom's compliance with GAAP. Defendant's motion for a new trial on this basis is denied.

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C. Limitations on the Use of Cynthia Cooper's Testimony

Defendant's final argument is that a new trial is necessary due to limitations that I placed on his use of documents relating to the Arthur Andersen audits. Defendant argues that these materials constituted hearsay admitted without objection from the Government, and therefore could have been used for any purpose, including as substantive proof that WorldCom's revenue accounting decisions conformed to GAAP. This argument lacks merit.

As a preliminary matter, Defendant misconstrues the trial record. As explained above, Defendant conceded that Cynthia Cooper's testimony regarding her delivery of Arthur Andersen audit opinions to Defendant was only "half the puzzle," that is, to show that Defendant "was aware that Arthur Andersen was auditing the books and records and gave clean bills of health every year." (Tr. 3167.) Defendant conceded that the other half of the puzzle — the use of the audit reports as substantive evidence of WorldCom's compliance with GAAP — "has to come through Ken Avery," Arthur Andersen's audit representative at WorldCom. (Tr. 3167.)

Having heard the parties' arguments about the admissibility and use of Ms. Cooper's testimony, I made the following ruling: "Certainly Ken Avery can talk about what he reviewed and what his opinion was about the accounting. Cynthia Cooper can talk about what she put together in packets and gave to the audit committee and the board that got to Bernie Ebbers." (Tr. 3169.) I thus permitted the admission of the audit reports through Ms. Cooper not for

the truth of what the reports asserted, but as evidence of Defendant's state of mind. This ruling comported with Defendant's position that testimony about the substance of Arthur Andersen's audit work must come from an Arthur Andersen witness. However, no such witness testified at trial. Defendant's claim that this evidence was admitted "without limitation" is therefore belied by both the record and his own proffers.

At a charging conference, Defendant changed course, asserting that because no limiting instruction was given when the audit reports were admitted through Ms. Cooper, he should be permitted to argue in summation that those reports are proof of WorldCom's GAAP compliance. (Tr. 3600-01.) I reiterated my ruling that these documents were admitted only as evidence of Defendant's state of mind. (Tr. 3601.)

Defendant's argument that he should have been given broad latitude to use the audit opinions based on their admission as hearsay also fails for the simple reason that these reports were not admitted as hearsay; their admission to show Defendant's state of mind is a non-hearsay purpose. Had Defendant called Ken Avery or another Arthur Andersen witness to testify to the truth of what the audit reports assert, a hearsay issue might have arisen. But he did not. Accordingly, Defendant's motion for a new trial on this basis is denied.

Appendix B

VI. Conclusion

For the foregoing reasons, Defendant's motion for a new trial is denied.

SO ORDERED:

s/ Barbara S. Jones
BARBARA S. JONES
UNITED STATES DISTRICT JUDGE

Dated: New York, New York
July 9, 2005

APPENDIX C — EXCERPTED TRIAL TRANSCRIPT (RULING RE DEFENDANT'S RENEWED MOTION FOR DEFENSE WITNESS IMMUNITY) DATED FEBRUARY 25, 2005

[3604]

* * *

I think it must be very apparent to the defense at this point that I'm not granting the motion to immunize Mr. Beaumont and Mr. Lomenzo or Ms. Scott, but let me deny your motion formally on the record.

I continue to believe the case law in the area is very clear. First and foremost, the choice on immunizing a potential witness lies with the executive branch.

Second, I can't find the government, and do not find the government has used immunity in this case to gain any tactical advantage over the defendant, so I don't think as a matter of law that the defendant has satisfied the first of the three prongs that have to be met before I would or could order immunity. But I want to add just a couple of things, now that I have the benefit of the record in the case, at least the government's case in chief.

It's clear to me that this case is very different from the situation that faced Judge Sweet in the DePalma case. Unlike in that case, in DePalma, the government in this case hasn't granted wide-reaching transactional immunity to the witnesses who provided the principal evidence against the defendant.

Appendix C

It also seems clear to me — and I think I said this earlier in a different context — that the testimony that could be offered, based on what I have seen, the 302, the proffer [3605] sessions of Beaumont, Lomenzo and Scott, is not testimony that directly exculpates Mr. Ebbers. Rather, to me it's an indication that they would offer self-exculpatory testimony. And I just don't think this justifies court-ordered immunity under the facts of this case.

* * *

APPENDIX D — ORDER OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK DATED NOVEMBER 10, 2004

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

S4 02 Cr. 1144 (BSJ)

UNITED STATES OF AMERICA,

v.

BERNARD J. EBBERS,

Defendant

ORDER

BARBARA S. JONES
UNITED STATES DISTRICT JUDGE

Defense Witness Immunity

Defendant Bernard J. Ebbers has moved for a court order compelling the government to grant immunity to two potential witnesses, Ronald Beaumont and Ronald Lomenzo, both former employees of WorldCom, Inc. ("WorldCom"), or face dismissal of the indictment. Alternatively, Defendant seeks an evidentiary hearing to determine whether such relief is appropriate. For the reasons set forth below, Defendant's motion is denied.

Appendix D

The decision whether to grant "[i]mmunity remains 'preeminently a function of the Executive Branch.'" *United States v. Salerno*, 937 F.2d 797, 807 (2d Cir. 1991) (quoting *United States v. Turkish*, 623 F.2d 769, 776 (2d Cir. 1980)). Courts have declined to find that the "Due Process Clause [] [imposes] a general requirement that defense witness immunity must be ordered whenever it seems fair to grant it." *United States v. Turkish*, 623 F.2d at 777. Therefore, "[t]his Circuit has followed the general rule that the United States ordinarily need not grant statutory immunity to a defense witness." *U.S. v. Praetorius*, 622 F.2d 1054, 1064 (2d Cir. 1979).

An exception to this general rule lies where a defendant fulfills the requirements of a three-part test fashioned by the Second Circuit. Under this test, the defendant bears the burden of showing that first, "the government has engaged in discriminatory use of immunity to gain a tactical advantage, or, through its own overreaching, has forced the witness to invoke the Fifth Amendment," second, that "the witness' testimony will be material, exculpatory and not cumulative," and third, that the testimony "is not obtainable from any other source." *United States v. Burns*, 684 F.2d 1066, 1077 (2d Cir. 1982). The Court finds that Defendant has failed to meet his burden on the first of these requirements, precluding the need for the Court to reach the second and third prongs of the test.

Defendant argues that the Government engaged in a discriminatory use of immunity by entering into agreements with five former WorldCom employees not to prosecute them

further in exchange for their guilty pleas and cooperation.[1] In addition, the government has entered into non-prosecution agreements with two other witnesses.[2] The Government has declined, however, to grant immunity to Mr. Ronald Beaumont, who served as COO of WorldCom, and to Mr. Ronald Lomenzo, WorldCom's former Senior Vice President of Financial Operations. Defendant relies on *United States v. Dolah*, 245 F.3d 98, 105-06 (2d Cir. 2001), for the proposition that the "discriminatory use" prong of the test "means simply a decision by the Government to confer immunity on some witnesses and not on others." *United States v. Dolah*, 245 F.3d 98, 105-06 (2d Cir. 2001). Because the Government has granted immunity to a handful of witnesses, but not to Beaumont and Lomenzo, Defendant contends that he has satisfied the first element of the *Burns* test.

The Court, however, finds that *Dolah* did not change the *Burns* standard and therefore that "tactical advantage" must accompany the government's discriminatory use of immunity to overcome that first hurdle. As Judge Haight found in considering *Dolah*, the Second Circuit "did not set any new standard for reviewing denials of immunity by prosecutors but rather summarized and affirmed existing precedent, in particular noting that interference with the power of prosecutors to grant or deny immunity was

1. The five WorldCom employees with whom the government has entered into such agreements are Scott Sullivan, David Myers, Buford Yates, Troy Norman and Betty Vinson.

2. The two witnesses with whom the government has entered non-prosecution agreements are Mark Abide and Sanjeev Sethi.

permissible only in 'limited circumstances.'" *United States v. Camacho*, 163 F.Supp.2d 287, 298 (S.D.N.Y. 2001) (quoting *Dolah*, 245 F.3d at 106). By citing *Dolah* as holding the government's discriminatory use of immunity to be sufficient, Defendant simply takes the words of the Second Circuit out of their proper context.

The Court finds none of the requisite tactical maneuvering by the Government to be present in this case. Defendant points to no prosecutorial misconduct or tactical moves, save the Government's decision not to immunize Mr. Beaumont or Mr. Lomenzo. However, that decision is "an everyday occurrence in criminal prosecutions," *United States v. Karlsen*, 2001 WL 428246, No. 00 Cr. 502, at *1 (S.D.N.Y. 2001), which is "preeminently a function of the Executive Branch." *United States v. Salerno*, 937 F.2d at 807 (2d Cir. 1991) (internal citation omitted). This conduct does not, by itself, implicate Defendant's constitutional right to a fair trial.

Moreover, even if the decision not to grant immunity to Mr. Beaumont and Mr. Lomenzo raised an inference of prosecutorial misconduct, the Government explains that it "has made decisions on whether to grant immunity to witnesses based on the particular circumstances of those witnesses and not in a discriminatory fashion to gain any tactical advantage." (Gov. Defense Witness Immunity Opposition Br. at 8.) Moreover, the ex parte declaration of Assistant United States Attorney Johnson supports this claim. In this regard, the instant case is distinguishable from *United States v. De Palma*, 476 F. Supp. 775 (S.D.N.Y. 1979), upon

which Defendant relies.[3] In *De Palma*, Judge Sweet found that the Government's denial of limited use immunity for two defense witnesses resulted in an unfair trial, in violation of the defendant's due process rights. The Government there granted transactional immunity to its key witness, the defendant's alleged co-conspirator. Judge Sweet found that "the foundation of the Government's case" against the defendant "was built by means of [that] far-reaching immunity grant." *United States v. De Palma*, 476 F. Supp. 775, 781 (S.D.N.Y. 1979). Indeed, the witness who received such broad immunity provided the "principal evidence" against the defendant. *Id.* at 777. Under those circumstances, the Government's "denial of limited use immunity for two defense witnesses resulted in an unfair trial." *Id.* at 781.

By contrast, the Government in this case has granted use immunity, rather than transactional immunity, to the five

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3. Also distinguishable is *United States v. Lord*, 711 F.2d 887 (9th Cir. 1983), where the Ninth Circuit remanded the case for an evidentiary hearing to determine whether "prosecutorial misconduct . . . could have prevented a defense witness from giving relevant testimony." *United States v. Lord*, 711 F.2d 887, 891 (9th Cir. 1983). In *Lord*, the defense witness at issue testified "that before trial the prosecutor told him that whether he would be prosecuted depended on his testimony," and the prosecutor "indicated that he told [the witness] about the self-incrimination privilege and that the government would not prosecute [him] if he submitted to an interview and testified truthfully." *Id.* The Ninth Circuit found that "both of these versions could suggest distortion of the judicial fact-finding process," necessitating an evidentiary hearing. *Id.* The Court would also note that the Ninth Circuit has adopted a different set of standards to assess motions to compel defense witness immunity, limiting the utility of *Lord*.

former WorldCom employees who are the principal witnesses in this case. In fact, all five of those employees have pled guilty to charges of conspiracy to commit securities fraud and securities fraud. On the other hand, the witnesses who have received non-prosecution agreements "are not expected to provide the foundation of the evidence of Ebber's participation in the fraudulent scheme charged in the Superceding Indictment." (Gov. Defense Witness Immunity Opposition Br. at 11.)

Finally, Defendant argues that Johnson's ex parte declaration "unfairly deprives Mr. Ebbers of the ability to respond to the government's secret evidence." (Reply Br. in Support of Defense Witness Immunity at 11.) However, in filing that ex parte declaration, the Government has followed the procedure set out by the Second Circuit in *United States v. Turkish*, 623 F.2d 769 (2d Cir. 1980) and reaffirmed in *United States v. Todaro*, 744 F.2d 5 (2d Cir. 1984). In the latter case, the Circuit Court explained:

> The prosecutor need only show that the witness has been indicted or present to the court in camera an ex parte affidavit setting forth the circumstances that support the prosecutor's suspicion of the witness's criminal activity. No duty is imposed upon the prosecutor; he simply has an option to rely upon the witness's status as an actual or potential target of prosecution to foreclose any inquiry concerning immunity for that witness.

Todaro, 744 F.2d at 9. The Court therefore views the Government's reliance upon Johnson's ex parte declaration as neither untoward nor unfair.

The Court finds that Defendant has failed to show that the Government has engaged in the tactical use of immunity or other forms of misconduct. Defendant therefore fails to carry his burden under the first prong of the *Burns* test. Accordingly, Defendant's motion for defense witness immunity or dismissal of the indictment is denied.

SO ORDERED:

s/ Barbara S. Jones
Barbara S. Jones
UNITED STATES DISTRICT JUDGE

Dated: New York, New York
November 10, 2004

APPENDIX E — CONSTITUTIONAL PROVISIONS, STATUTES, AND REGULATIONS INVOLVED

UNITED STATES CONSTITUTION

Amendment V [1791]

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

Amendment VI [1791]

In all criminal prosecutions, the accused shall enjoy the right to a speedy and public trial, by an impartial jury of the State and district wherein the crime shall have been committed, which district shall have been previously ascertained by law, and to be informed of the nature and cause of the accusation; to be confronted with the witnesses against him; to have compulsory process for obtaining witnesses in his favor, and to have the Assistance of Counsel for his defence.

Appendix E

STATUTES

15 U.S.C.S. § 78ff

§ 78ff. Penalties

(a) Willful violations; false and misleading statements. Any person who willfully violates any provision of this chapter (other than section 78dd-1 of this title), or any rule or regulation thereunder the violation of which is made unlawful or the observance of which is required under the terms of this chapter, or any person who willfully and knowingly makes, or causes to be made, any statement in any application, report, or document required to be filed under this chapter or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 78o of this title, or by any self-regulatory organization in connection with an application for membership or participation therein or to become associated with a member thereof, which statement was false or misleading with respect to any material fact, shall upon conviction be fined not more than $5,000,000, or imprisoned not more than 20 years, or both, except that when such person is a person other than a natural person, a fine not exceeding $25,000,000 may be imposed; but no person shall be subject to imprisonment under this section for the violation of any rule or regulation if he proves that he had no knowledge of such rule or regulation.

(b) Failure to file information, documents, or reports. Any issuer which fails to file information, documents, or reports required to be filed under subsection (d) of section 78o of this title or any rule or regulation thereunder shall forfeit to the United States the sum of $100 for each and every day such failure to file shall continue. Such forfeiture, which shall be in lieu of any criminal penalty for such failure to file which might be deemed to arise under subsection (a) of this section, shall be payable into the Treasury of the United States and shall be recoverable in a civil suit in the name of the United States.

(c) Violations by issuers, officers, directors, stockholders, employees, or agents of issuers

(1)(A) Any issuer that violates subsection (a) or (g) of section 78dd-1 of this title shall be fined not more than $2,000,000.

(B) Any issuer that violates subsection (a) or (g) of section 78dd-1 of this title shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Commission.

(2)(A) Any officer, director, employee, or agent of an issuer, or stockholder acting on behalf of such issuer, who willfully violates subsection (a) or (g) of section 78dd-1 of this title shall be fined not more than $100,000, or imprisoned not more than 5 years, or both.

(B) Any officer, director, employee, or agent of an issuer, or stockholder acting on behalf of such issuer, who violates subsection (a) or (g) of section 78dd-1 of this title shall be subject to a civil penalty of not more than $10,000 imposed in an action brought by the Commission.

(3) Whenever a fine is imposed under paragraph (2) upon any officer, director, employee, agent, or stockholder of an issuer, such fine may not be paid, directly or indirectly, by such issuer.

15 U.S.C.S. § 78j

§ 78j. Manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

(a)(1) To effect a short sale, or to use or employ any stop-loss order in connection with the purchase or sale, of any security registered on a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(2) Paragraph (1) of this subsection shall not apply to security futures products.

> (b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement (as defined in section 206B of the Gramm-Leach-Bliley Act), any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Rules promulgated under subsection (b) of this section that prohibit fraud, manipulation, or insider trading (but not rules imposing or specifying reporting or recordkeeping requirements, procedures, or standards as prophylactic measures against fraud, manipulation, or insider trading), and judicial precedents decided under subsection (b) of this section and rules promulgated thereunder that prohibit fraud, manipulation, or insider trading, shall apply to security-based swap agreements (as defined in section 206B of the Gramm-Leach-Bliley Act) to the same extent as they apply to securities. Judicial precedents decided under section 77q(a) of this title and sections 78i, 78o, 78p, 78t, and 78u-1 of this title, and judicial precedents decided under applicable rules promulgated under such sections, shall apply to security-based swap agreements (as defined in section 206B of the Gramm-Leach-Bliley Act) to the same extent as they apply to securities.

Appendix E

15 U.S.C.S. § 78m

§ 78m. Periodical and other reports

(a) Reports by issuer of security; contents. Every issuer of a security registered pursuant to section 78l of this title shall file with the Commission, in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate for the proper protection of investors and to insure fair dealing in the security—

(1) such information and documents (and such copies thereof) as the Commission shall require to keep reasonably current the information and documents required to be included in or filed with an application or registration statement filed pursuant to section 78l of this title, except that the Commission may not require the filing of any material contract wholly executed before July 1, 1962.

(2) such annual reports (and such copies thereof), certified if required by the rules and regulations of the Commission by independent public accountants, and such quarterly reports (and such copies thereof), as the Commission may prescribe.

Every issuer of a security registered on a national securities exchange shall also file a duplicate original of such information, documents, and reports with the exchange.

* * * *

Appendix E

18 U.S.C.S. § 2

§ 2. Principals

(a) Whoever commits an offense against the United States or aids, abets, counsels, commands, induces or procures its commission, is punishable as a principal.

(b) Whoever willfully causes an act to be done which if directly performed by him or another would be an offense against the United States, is punishable as a principal.

18 U.S.C.S. § 371

§ 371. Conspiracy to commit offense or to defraud United States

If two or more persons conspire either to commit any offense against the United States, or to defraud the United States, or any agency thereof in any manner or for any purpose, and one or more of such persons do any act to effect the object of the conspiracy, each shall be fined under this title or imprisoned not more than five years, or both.

If, however, the offense, the commission of which is the object of the conspiracy, is a misdemeanor only, the punishment for such conspiracy shall not exceed the maximum punishment provided for such misdemeanor.

Appendix E

18 U.S.C.S. § 6001

§ 6001. Definitions

As used in this chapter—

(1) "agency of the United States" means any executive department as defined in section 101 of title 5, United States Code, a military department as defined in section 102 of title 5, United States Code, the Nuclear Regulatory Commission, the Board of Governors of the Federal Reserve System, the China Trade Act registrar appointed under 53 Stat. 1432 (15 U.S.C. sec. 143), the Commodity Futures Trading Commission, the Federal Communications Commission, the Federal Deposit Insurance Corporation, the Federal Maritime Commission, the Federal Power Commission, the Federal Trade Commission, the Surface Transportation Board, the National Labor Relations Board, the National Transportation Safety Board, the Railroad Retirement Board, an arbitration board established under 48 Stat. 1193 (45 U.S.C. sec. 157), the Securities and Exchange Commission, or a board established under 49 Stat. 31 (15 U.S.C. sec. 715d);

(2) "other information" includes any book, paper, document, record, recording, or other material;

(3) "proceeding before an agency of the United States" means any proceeding before such an agency with respect to which it is authorized to issue subpenas and to take testimony or receive other information from witnesses under oath; and

(4) "court of the United States" means any of the following courts: the Supreme Court of the United States, a United States court of appeals, a United States district court established under chapter 5, title 28, United States Code, a United States bankruptcy court established under chapter 6, title 28, United States Code, the District of Columbia Court of Appeals, the Superior Court of the District of Columbia, the District Court of Guam, the District Court of the Virgin Islands, the United States Court of Federal Claims, the Tax Court of the United States, the Court of International Trade, and the Court of Appeals for the Armed Forces.

Appendix E

18 U.S.C.S. § 6002

§ 6002. Immunity generally

Whenever a witness refuses, on the basis of his privilege against self-incrimination, to testify or provide other information in a proceeding before or ancillary to—

(1) a court or grand jury of the United States,

(2) an agency of the United States, or

(3) either House of Congress, a joint committee of the two Houses, or a committee or a subcommittee of either House,

and the person presiding over the proceeding communicates to the witness an order issued under this title, the witness may not refuse to comply with the order on the basis of his privilege against self-incrimination; but no testimony or other information compelled under the order (or any information directly or indirectly derived from such testimony or other information) may be used against the witness in any criminal case, except a prosecution for perjury, giving a false statement, or otherwise failing to comply with the order.

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18 U.S.C.S. § 6003

§ 6003. Court and grand jury proceedings

(a) In the case of any individual who has been or may be called to testify or provide other information at any proceeding before or ancillary to a court of the United States or a grand jury of the United States, the United States district court for the judicial district in which the proceeding is or may be held shall issue, in accordance with subsection (b) of this section, upon the request of the United States attorney for such district, an order requiring such individual to give testimony or provide other information which he refuses to give or provide on the basis of his privilege against self-incrimination, such order to become effective as provided in section 6002 of this title.

(b) A United States attorney may, with the approval of the Attorney General, the Deputy Attorney General, the Associate Attorney General, or any designated Assistant Attorney General or Deputy Assistant Attorney General, request an order under subsection (a) of this section when in his judgment—

(1) the testimony or other information from such individual may be necessary to the public interest; and

(2) such individual has refused or is likely to refuse to testify or provide other information on the basis of his privilege against self-incrimination.

Appendix E

REGULATIONS

17 C.F.R. 240.10b-5

§ 240.10b-5 Employment of manipulative and deceptive devices.

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

Appendix E

17 C.F.R. 240.13a-1

§ 240.13a-1 Requirements of annual reports.

Every issuer having securities registered pursuant to section 12 of the Act (15 U.S.C. 78l) shall file an annual report on the appropriate form authorized or prescribed therefor for each fiscal year after the last full fiscal year for which financial statements were filed in its registration statement. Annual reports shall be filed within the period specified in the appropriate form.

APPENDIX F — EXCERPTS FROM TRIAL TRANSCRIPT RE: CHARGE CONFERENCE DATED FEBRUARY 25, 2005

[Commencing at page 3568]

* * *

MR. ANDERS: And I was at least considering not pursuing the conscious avoidance. I wanted to think about it some more, and honestly I haven't had a chance to.

THE COURT: It sounds like we may all be sort of in the same place. I don't think I can decide this until I hear Mr. Ebbers's testimony.

MR. ANDERS: I can articulate a basis, just to amplify a little bit, where there are certainly situations where it could be that he stuck his head in the sand, for lack of a better term, and he was presented with this information. And if he deliberately avoided knowing what was put in front of him, that's conscious avoidance, and that could be both with the line costs and the revenue case.

He was shown documents which had both large line cost adjustments, and the revenue decks show what we claim is the true operating performance of the company, and then the public sees completely different information.

If the defense is I didn't know what the real business was, I only knew what was in the financial statements, we would articulate that there is at least a theory for he consciously avoided knowing the true financial condition of the company, notwithstanding it was right in front of him.

THE COURT: My fear, having read these cases, is that [3569] the Circuit would say is what that argument really is is proof that he knew, not proof that he avoided.

MR. ANDERS: I agree there is a step missing. That's the part where I don't know what he is going to say.

MR. HEBERLIG: Or he should have known and was negligent. Either way it's an improper instruction.

THE COURT: All right. Well, look, we have to wait until we have heard his testimony.

* * * *

APPENDIX G — EXCERPTS FROM TRIAL TRANSCRIPT RE: RULING RE CONSCIOUS AVOIDANCE CHARGE DATED MARCH 2, 2005

[Commencing at page 4103]

* * *

THE COURT: Everyone did make their arguments on conscious avoidance last night. I would like to supplement the record with my thinking for the simple reason that I think I [4104] have given one conscious avoidance charge in ten years. This will he the second. I think it's important to state on the record why under the facts of this particular case it's appropriate.

Obviously, the law is that it's appropriate where the element of knowledge is in dispute. Clearly we have a dispute among the parties there. Mr. Ebbers' knowledge is in dispute. And, two, that the evidence would permit a rational juror to conclude beyond a reasonable doubt that the defendant was aware of a high probability of the fact in dispute and consciously avoided confirming that fact.

As I think the government alluded to yesterday, the conscious avoidance charge and the entitlement to it was not nearly so clear, if made out at all, prior to Mr. Ebbers' testimony. However, now that he has testified, I find that the second requirement has been fulfilled, and I am using the standard articulated by the Second Circuit in the Svoboda case, which was that the defendant's involvement in the criminal offense was so overwhelmingly suspicious that the defendant's failure to question the suspicious circumstances

establishes the defendant's purposeful contrivance to avoid guilty knowledge.

I want to go through just a few facts that a rational juror could find that would result in such a finding. They include these facts, but this is not meant to be an exhaustive [4105] list.

Essentially, the defendant conceded that he saw a number of documents, including management budget variance reports, close the gap presentations and mon rev reports.

There is no dispute, and the defendant conceded, that line costs are the largest expense of the company.

He also testified the September management budget variance report, which was primarily a report of SG&A expenses, was created exclusively for him. He admitted he focused on the SG&A expenses listed in that report, but a few lines from the SG&A expenses, which the defendant testified he focused, that report showed line costs, in the particular instance that was gone over on cross-examination, of $700 million, which was a significant variance from the 1.4 billion that was budgeted for that month. He testified he saw neither that item nor the gross margin figure of 78 percent.

He testified in February 2001 he attended a dinner with Scott Sullivan, Ron Beaumont, Tom Bosley where, quote, the comment was made that we need to do everything we can to put in programs to lower line costs because these costs were not coming down as fast as we thought they should.

This statement a reasonable juror could find reveals that as of that time, the defendant had some knowledge of rising line costs. Yet he testified that as of the first quarter of 2001, he didn't look at the management budget variance report that showed the line [4106] cost adjustments. He testified, in fact, that he probably threw it in the trash.

The defendant testified he attended line cost meetings and at one such meeting he was told that capital expenditures were 2 to $2-1/2 billion over maintenance capital expenditures. And that he was provided a partial explanation by Scott Sullivan, but did not ask any further questions about the source of the extra expenditures.

The defendant admitted that fraudulently reducing line costs and capitalizing them would affect the accuracy of EBITDA, earnings per share, and net income, all of which were reported to the public by him, both in SEC filings and in various other forms, like conference calls and at meetings.

As I said, these are just a few of the facts that I think entitle the government to the conscious avoidance charge. It's not meant to be exhaustive.

All right. Anything else?

* * * *

APPENDIX H — EXCERPTS FROM TRIAL TRANSCRIPT RE: CONSCIOUS AVOIDANCE CHARGE IN JURY INSTRUCTIONS DATED MARCH 4, 2005

[Commencing at page 4444]

* * *

Now, with respect to Counts Two and Three through Nine, in determining whether the defendant knew of the existence of a particular fact, you may consider whether the defendant deliberately closed his eyes to what otherwise would have been obvious.

The necessary knowledge on the part of the defendant with respect to Count Two and Counts Three through Nine cannot be established by showing that the defendant was careless, negligent, or foolish. In addition, you may not conclude that the defendant knew of the existence of a particular fact merely because he held the position of chief executive at WorldCom. However, one may not willfully and intentionally remain ignorant of a fact material and important to his conduct in order to escape the consequences of criminal law.

Thus, if you find beyond a reasonable doubt that the defendant was aware that there was a high probability of a fact, but that the defendant deliberately and consciously avoided confirming this fact, then you may treat this [4445] deliberate avoidance of positive knowledge as the equivalent of knowledge, unless you find that the defendant actually believed the fact not to be true.

* * *

Appendix H

If you determine that the conspiracy had unlawful objects, in determining whether the defendant joined the conspiracy with knowledge of those unlawful objectives, you may consider whether the defendant deliberately closed his eyes to what otherwise would have been obvious. The necessary knowledge however, cannot be established by showing that the defendant was careless, negligent, or foolish. However, one may not willfully and intentionally remain ignorant of a fact material and important to his own conduct in order to escape the consequences of criminal law. If you find beyond a reasonable doubt that the defendant was aware of a high probability that any object or objects you have already found existed — securities fraud, false or misleading statements in financial statements, or the falsification of the books and records of a public company -- but deliberately and consciously avoided confirming their existence, then you may treat this deliberate avoidance of positive knowledge as the equivalent of knowledge, unless you find that the defendant actually believed that these objects did not exist.

* * * *